

ORDER NO. 6399

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Before Commissioners:

Michael Kubayanda, Chairman;
Mark Acton, Vice Chairman;
Ann C. Fisher;
Ashley E. Poling; and
Robert G. Taub

Institutional Cost Contribution
Requirement for Competitive Products

Docket Nos. RM2017-1
RM2022-2

ORDER FINALIZING RULE RELATING TO THE INSTITUTIONAL
COST CONTRIBUTION REQUIREMENT FOR COMPETITIVE PRODUCTS



Washington, DC 20268-0001

January 9, 2023

TABLE OF CONTENTS

	<i>Page</i>
I. Introduction.....	1
II. Procedural History.....	2
III. Overview	4
A. Background and Remand	4
B. Overview of Supplemental Notice of Proposed Rulemaking.....	9
C. Final Rule.....	15
IV. Statutory Interpretation of 39 U.S.C. Chapter 36	18
A. Background.....	18
B. Cost Allocation is Not the Appropriate Share Provision's Primary Purpose	23
1. Comments.....	23
2. Commission Analysis	26
C. Preventing Subsidization is Not the Appropriate Share Provision's Primary Purpose	46
1. Comments.....	46
2. Commission Analysis	48
D. The Objective Appearing in 39 U.S. Code Section 3622(b) is Not Relevant to the Appropriate Share Review	53
1. Comments.....	53
2. Commission Analysis	53
E. Prior Commission Statements Do Not Foreclose Use of the Dynamic Formula-Based Approach	54
1. Comments.....	54
2. Commission Analysis	54
F. The Commission Properly Considered the Degree to Which Any Costs are Uniquely or Disproportionately Associated with Any Competitive Products	57
1. Comments.....	57
2. Commission Analysis	59
G. The Commission Reasonably Followed the Court's Instruction to Consider Both Institutional and Attributable Costs	65

1.	Comments.....	65
2.	Commission Analysis	74
V.	Commission Analysis of All Relevant Circumstances.....	75
A.	Uniquely or Disproportionately Associated Costs	76
1.	Background.....	76
2.	The Commission Considered the Degree to Which Any Costs are Uniquely or Disproportionately Associated with Any Competitive Products.....	83
3.	The Commission Considered the Potential Need for the Appropriate Share to Ameliorate an Alleged Deficit Left by the Use of the Incremental Costs Test	89
4.	The Commission Considered Incorporating Attributable Costs into the Minimum Contribution Requirement (With and Without Double-Counting)	93
5.	The Commission Considered the Existence of Uniquely or Disproportionately Associated Costs within Institutional Costs	96
6.	The Commission Considered Whether to Incorporate Unattributed Inframarginal Costs into the Minimum Contribution Requirement .	99
7.	The Commission's Use of Sound Economic Measurement is Reasonable	102
8.	The Commission Rejects the Arbitrary Allocation of Institutional Costs to Market Dominant versus Competitive Products as Unreasonable.....	106
B.	The Prevailing Competitive Conditions in the Market and Other Relevant Circumstances	112
1.	Background.....	112
2.	The Current State of Competition in the Market for Competitive Postal Services Remains Healthy	125
3.	The Commission Considered Circumstances Alleged by Commenters to be Relevant Under 39 U.S.C. § 3633(b)	140
4.	The Formula is a Reasonable Approach to Setting the Minimum Contribution Requirement	154
VI.	Commission Analysis Pursuant to Uncodified Section 703(d) of the PAEA.....	165
A.	Introduction	165
B.	Comments	170

C.	Commission Analysis.....	172
VII.	Commission Consideration of Specific Costs Raised by Commenters.....	177
A.	Background.....	177
B.	Costs Specifically Addressed in Order No. 6043	179
1.	New Vehicle Purchases	181
2.	City Carrier Assistant Costs	197
3.	Headquarters and Management Costs	203
4.	Supply Personnel and City Carrier Street Time	207
5.	Package Processing and Delivery Technology	210
C.	Additional Costs Raised by Commenters.....	212
1.	Peak Season Costs.....	214
2.	Rural Carrier Costs and Vehicle Service Driver Costs	217
3.	Other Types of Costs	218
VIII.	Alternatives Raised by Commenters	225
A.	Attributable Cost Shares	225
1.	Introduction	225
2.	Comments.....	226
3.	Commission Analysis	229
B.	Reference to Market Dominant Contribution.....	239
1.	Introduction	239
2.	Comments.....	239
3.	Commission Analysis	242
C.	Stand-Alone Market Dominant Costs.....	247
1.	Introduction	247
2.	Comments.....	248
3.	Commission Analysis	251
D.	Regression-Based Approach	255
1.	Introduction	255
2.	Comments.....	256
3.	Commission Analysis	260
E.	Elimination of the Appropriate Share	265

1.	Introduction	265
2.	Comments.....	267
3.	Commission Analysis	268
IX.	Regulatory Flexibility Act Analysis.....	270
X.	Ordering Paragraphs	271

Attachment—Final Rule

Appendix A—Initial, Reply, and Section 703 Comments and Related Filings

Appendix B—Motions Practice and Related Filings

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(Issued January 9, 2023)

I. INTRODUCTION

The United States Court of Appeals for the District of Columbia Circuit remanded Docket No. RM2017-1 to the Commission for further consideration consistent with the opinion issued in *United Parcel Service, Inc. v. Postal Regulatory Commission*, 955 F.3d 1038 (D.C. Cir. 2020).¹ This Order resolves the issues identified by the court and concludes the Commission's third 5-year review of the institutional cost contribution requirement for Competitive products, which is also referred to as "the appropriate

¹ The Commission refers to this decision as "*UPS II*" to differentiate it from *United Parcel Serv., Inc. v. Postal Regul. Comm'n*, 890 F.3d 1053 (D.C. Cir. 2018), reh'rg *en banc* denied, (D.C. Cir. Jul. 27, 2018); cert. denied, 139 S.Ct. 2614 (May 20, 2019), which is referred to as "*UPS I*".

share,” in accordance with the requirements of 39 U.S.C. § 3633(a)(3) and (b). Based on the analysis provided below and review of comments, the Commission readopts its dynamic formula-based approach to calculating the appropriate share. The text of final 39 C.F.R. § 3035.107(c) appears in the Attachment to this Order.

II. PROCEDURAL HISTORY

On November 22, 2016, the Commission initiated Docket No. RM2017-1 by issuing Order No. 3624.² Order No. 3624 served as an advance notice of proposed rulemaking and provided an opportunity for interested persons to file initial comments and reply comments concerning the Commission’s second 5-year review of the appropriate share as required by 39 U.S.C. § 3633(b). See *generally* Order No. 3624. On February 8, 2018, the Commission issued Order No. 4402, which considered all of the comments that were filed and proposed a new formula-based approach to setting the appropriate share.³ On August 7, 2018, the Commission issued Order No. 4742, which was a revised notice of proposed rulemaking that addressed commenters’ concerns, proposed modifications to the formula-based approach, and provided for an additional comment period.⁴ On January 3, 2019, the Commission issued Order No. 4963, which analyzed all comments filed in response to Order No. 4742 and

² Advance Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products, November 22, 2016 (Order No. 3624). The Advance Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products was published in the *Federal Register* on November 29, 2016. See 81 Fed. Reg. 85,906 (Nov. 29, 2016).

³ Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products, February 8, 2018 (Order No. 4402). The Notice of Proposed Rulemaking was published in the *Federal Register* on February 14, 2018. See 83 Fed. Reg. 6758 (Feb. 14, 2018).

⁴ Revised Notice of Proposed Rulemaking, August 7, 2018 (Order No. 4742). The Revised Notice of Proposed Rulemaking was published in the *Federal Register* on August 13, 2018. See 83 Fed. Reg. 39,939 (Aug. 13, 2018).

adopted the final rule implementing the dynamic formula-based approach.⁵ Order No. 4963 was remanded to the Commission by the United States Court of Appeals for the District of Columbia Circuit for further consideration of certain discrete issues.⁶

On November 18, 2021, the Commission issued Order No. 6043, which was a supplemental notice of proposed rulemaking that addressed the issues identified by the court and provided an opportunity for interested persons to file initial comments and reply comments concerning the Commission's third 5-year review of the appropriate share as required by 39 U.S.C. § 3633(b).⁷ In response to Order No. 6043, 9 commenters participated by filing 14 sets of initial/reply comments, along with 4 declarations/reports, and 6 library references.⁸

On September 7, 2022, the Commission issued Order No. 6269, which invited public comment relating to the Commission's analysis pursuant to uncodified section 703(d) of the Postal Accountability and Enhancement Act (PAEA).⁹ On September 21, 2022, six comments were filed in response to Order No. 6269.¹⁰ Additionally on September 30, 2022, the Postal Service submitted reply comments, along with a motion for leave to file reply comments addressing concerns raised by UPS. Postal Service 703(d) Reply Comments, Postal Service Motion for Leave. The Commission finds that

⁵ Order Adopting Final Rules Relating to the Institutional Cost Contribution Requirement for Competitive Products, January 3, 2019 (Order No. 4963). The Final Rulemaking was published in the *Federal Register* on January 31, 2019. See 84 Fed. Reg. 537 (Jan. 31, 2019).

⁶ *UPS II*, 955 F.3d 1038, No. 19-1026, ECF Document No. 1846181, June 8, 2020, at 1 (issuing formal mandate) (ECF Document No. 1846181).

⁷ Supplemental Notice of Proposed Rulemaking and Order Initiating the Third Review of the Institutional Cost Contribution Requirement for Competitive Products, November 18, 2021 (Order No. 6043). The Supplemental Notice of Proposed Rulemaking was published in the *Federal Register* on August 13, 2018. See 86 Fed. Reg. 67,882 (Nov. 30, 2021).

⁸ Appendix A lists the citations to these filings, organized by commenter.

⁹ Notice and Order Providing an Opportunity to Comment on the Commission's Section 703(d) Analysis, September 7, 2022 (Order No. 6269); Postal Accountability and Enhancement Act (PAEA), Pub. L. No. 109-435, Title VII, § 703, 120 Stat. 3198, 3244 (2006).

¹⁰ Appendix A lists the citations to these filings, organized by commenter.

accepting and considering the Postal Service 703(d) Reply Comments would not prejudice any party and the unopposed Motion for Leave is granted. The Commission resolved four motions for access to non-public materials pursuant to 39 C.F.R. § 3011.301(e) and United Parcel Service, Inc. (UPS) responded to a Chairman's Information Request containing questions proposed by the Postal Service pursuant to 39 C.F.R. § 3010.170(b)(2) and (c).¹¹ This Order analyzes these filings where relevant to the issues presented.

III. OVERVIEW

A. Background and Remand

The PAEA requires that the Postal Service's Competitive products collectively cover what the Commission determines to be an appropriate share of the Postal Service's institutional costs. 39 U.S.C. § 3633(a)(3). The Commission implemented this requirement in 2007 by issuing Order No. 43, which set the initial appropriate share level at a static 5.5 percent.¹²

The PAEA also requires that the Commission revisit its regulations concerning the appropriate share at least every 5 years to determine if the minimum contribution requirement should be "retained in its current form, modified, or eliminated."¹³ In making such a determination, the Commission must consider "all relevant

¹¹ Appendix B lists the citations to these filings, organized by subject.

¹² See Docket No. RM2007-1, Order Establishing Ratemaking Regulations for Market Dominant and Competitive Products, October 29, 2007, at 91, 138 (Order No. 43).

¹³ 39 U.S.C. § 3633(b). As the Commission has long recognized, 39 U.S.C. § 3633 permits the Commission, if necessary, to revisit the appropriate share more often than once every 5 years. See Docket No. RM2012-3, Order Granting, In Part, Motion of the Parcel Shippers Association to Extend Period for Comments, March 7, 2012, at 4 (Order No. 1276) ("The PAEA . . . specifically authorizes the Commission to revise its competitive product rules from 'time to time[,]' . . . [t]hus, the Commission is not limited to reviewing competitive products' contribution at 5 year intervals."). This means that the Commission never lacks jurisdiction to review the appropriate share.

circumstances, including the prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products.” 39 U.S.C. § 3633(b). After completing its first 5-year review of the appropriate share as required by 39 U.S.C. § 3633(b) in 2012, the Commission issued Order No. 1449, which retained the appropriate share level of 5.5 percent.¹⁴

The Commission undertook its second 5-year review of the appropriate share in 2017 in Docket No. RM2017-1. Order No. 4963 finalized rule changes ending the use of the static 5.5 percent of institutional costs as the standard to calculate the appropriate share. *See generally* Order No. 4963. Instead, Order No. 4963 adopted and codified a new methodology to calculate the appropriate share: a dynamic formula-based approach that measures aspects of the competitive market and updates the appropriate share, based on market changes, on an annual basis.¹⁵

UPS challenged Order No. 4963, arguing, among other things, that the Commission did not consider costs “uniquely or disproportionately associated” with Competitive products.¹⁶ Additionally, UPS argued that the Commission’s dynamic formula-based approach to calculating the appropriate share rested on an improper assumption that unfair competition is impossible and used variables and weighting that lacked a rational explanation. *See* UPS Brief at 3-4, 5, 18-20. The United States Court of Appeals for the District of Columbia Circuit remanded Order No. 4963 to the

¹⁴ See Docket No. RM2012-3, Order Reviewing Competitive Products’ Appropriate Share Contribution to Institutional Costs, August 23, 2012 (Order No. 1449).

¹⁵ *See generally id.* Initially, this new methodology was codified at 39 C.F.R. § 3015.7(c). *See* Order No. 4963 at 188, Attachment A at 1-2. Prior to the issuance of the *UPS II* decision, this rule was redesignated as 39 C.F.R. § 3035.107(c). *See* Docket No. RM2019-13, Order Reorganizing Commission Regulations and Amending Rules of Practice, January 16, 2020, at 26, App’x A at 6 (Order No. 5407). *See also* 85 Fed. Reg. 9,614, 9,615 (Feb. 19, 2020) (final rule).

¹⁶ *See* Brief for Petitioner United Parcel Service, Inc., *UPS II*, 955 F.3d 1038, No. 19-1026, ECF Document No. 1814771, at 3, 5, 17-18, finalized November 7, 2019 (UPS Brief).

Commission for further consideration. See ECF Document No. 1846181. The court identified two major aspects of Order No. 4963 for the Commission to clarify on remand.

First, the court found that “the Commission ha[d] not adequately explained how the statutory phrases ‘direct and indirect postal costs attributable to [a particular competitive] product through reliably identified causal relationships’ and ‘costs . . . uniquely or disproportionately associated with any competitive products’ can coincide.” *UPS II*, 955 F.3d at 1041, 1049. The court stated that “the Commission cannot simply *assume* that the ‘uniquely or disproportionately associated with’ standard is subsumed by the ‘reliably identified causal relationships’ standard[.]” because doing so “would impermissibly conflate the language of § 3633(a)(2)—which incorporates the definition of ‘costs attributed’ from § 3631(b)—with the evidently distinct language of § 3633(b).” *Id.* at 1049 (emphasis in original). The court specified that the Commission “must explain why these two statutory phrases have the same practical reach despite the use of different language.” *Id.*

Second, the court found that “in focusing narrowly on costs attributed to competitive products under [39 U.S.C.] § 3633(a)(2), the Commission failed to discharge its responsibility under [39 U.S.C.] § 3633(b) to ‘consider . . . the degree to which *any* costs are uniquely or disproportionately associated with any competitive products.’” *Id.* at 1042, 1049 (emphasis in original). The court indicated that this “includes, but is not limited to, any costs [uniquely or disproportionately associated with Competitive products] that the Commission may have already considered when it promulgated regulations under § 3633(a)(1) or § 3633(a)(2).” *Id.* at 1050.

The court also supplied two examples of outstanding issues that the Commission should address on remand and which “illustrate[d] some of what a fuller ‘consider[ration]’ of the relevant costs [would] involve.” *Id.* at 1051.

First, the court stated that “the Commission should fully address the issue left open in [*UPS I*].” *Id.* at 1051. In *UPS I*, the court upheld Final Order No. 3506,¹⁷ in which the Commission declined to attribute all inframarginal costs to products under section 3633(a)(2) (as proposed by UPS), and instead adopted an expanded definition of costs attributable under the same causation-based approach, which allowed the attribution of some inframarginal costs to products. *See UPS I*, 890 F.3d at 1058-59, 1069. In responding to an argument that Final Order No. 3506 had been arbitrary and capricious in failing to explain how the new attribution standard served relevant statutory objectives with respect to fair competition, the court agreed with the Commission that “[t]he purpose of [cost attribution under 39 U.S.C. § 3633(a)(2)] is not to ensure that the Postal Service is competing fairly,’ but rather . . . to ‘ensure that products cover all of the costs the Postal Service incurs in providing them,’ which in turn plays but a contributing role in the statute’s overall pro-competitive aims.” *Id.* at 1067 (citation omitted). The court stated that the petitioner “offer[ed] no reason to doubt that the [PAEA’s] prohibition on cross-subsidization[] [under 39 U.S.C. § 3633(a)(1)][] and requirement that [C]ompetitive products cover a share of institutional costs [under 39 U.S.C. § 3633(a)(3)][] [would] adequately ameliorate any competitive deficit left by the Commission’s approach to cost attribution” *Id.*

¹⁷ See Docket No. RM2016-2, Order Concerning United Parcel Service, Inc.’s Proposed Changes to Postal Service Costing Methodologies (UPS Proposals One, Two, and Three), September 9, 2016 (Order No. 3506). The Commission filed an errata updating Order No. 3506. Docket No. RM2016-2, Notice of Errata, October 19, 2016. The version of Order No. 3506 that includes the corrected pages is hereafter referred to as “Final Order No. 3506.”

In *UPS II*, the court stated that:

The court in [*UPS I*] recognized that, because the costs attributed test under § 3633(a)(2) is conservative, there may be institutional costs that are ‘uniquely or disproportionately associated with competitive products,’ even though they cannot be said to stand in ‘reliably identified causal relationships’ with them. [Order No. 4963] does not address this.

UPS II, 955 F.3d at 1051. The court further states that this approach to cost attribution “leaves open important questions,” such as:

Are some of the Postal Service’s institutional costs – and especially its unattributed inframarginal costs – still related in some meaningful way to competitive products, even if those costs cannot be attributed under § 3633(a)(2)? And if so – if, for instance, some of those institutional costs are ‘uniquely or disproportionately associated with competitive products,’ 39 U.S.C. § 3633(b) – might they need to be accounted for when the Commission issues regulations under another provision of the Accountability Act?

Id. at 1045. The court directed the Commission to address these questions on remand.

Second, the court stated that the Commission “must explain the relevance (if any) of costs it may have considered in implementing § 3633(a)(1)[,]” to the extent that any such costs are critical to the Commission’s analysis under section 3633(a)(3). *Id.* at 1051. The court recognized “that the Commission might decide against revising its bottom-line judgment, [to adopt the dynamic formula-based approach to calculating the appropriate share] given the other factors the Commission must consider under § 3633(b) and the latitude that the text affords the Commission in making a final determination.” *Id.*

After issuing Order No. 4963, the Commission continued to calculate the appropriate share using its dynamic formula and published updated calculations

annually in its *Annual Compliance Determination* (ACD) reports.¹⁸ Due to the appellate proceedings, the Commission also analyzed the Postal Service's compliance with 39 U.S.C. § 3633(a)(3) in accordance with the prior appropriate share requirement set at the static 5.5 percent. See n.18, *supra*. The Postal Service has continued to exceed both the prior appropriate share requirement of 5.5 percent and the dynamic formula-based calculation. See *id.*; see also Section V.B.2.b., *supra*, Table V-7.

B. Overview of Supplemental Notice of Proposed Rulemaking

In Order No. 6043 the Commission addressed the issues identified by the D.C. Circuit in its remand opinion and initiated the third statutorily-required 5-year review of the institutional cost contribution requirement for Competitive products, in accordance with the requirements of 39 U.S.C. § 3633(a)(3) and (b). The Commission first provided necessary background concerning the Commission's cost attribution ("costing") methodology and how that methodology has evolved over time. Order No. 6043 at 11-40. As the Commission explained, the current costing methodology is designed to facilitate the attribution of costs to products or groups of products to the greatest extent feasible. *Id.* at 11-34. The Commission discussed the nature of institutional costs and why they cannot be allocated any further. *Id.* at 34-35. With respect to Competitive product regulation, the Commission explained how section 3633, as currently implemented by the Commission, functionally results in a series of interrelated price floors. *Id.* at 22-35. The price floor required by 39 U.S.C. § 3633(a)(2), which requires each Competitive product to recover its product-level attributable costs, is included in the calculation of the price floor under 39 U.S.C. § 3633(a)(1), which requires the

¹⁸ The formula is recursive, to incorporate year-over-year changes in the market for competitive postal services; thus, the Commission has continued to update and publish the relevant calculations. See Docket No. ACR2021, *Annual Compliance Determination*, March 29, 2022, at 96-100 (FY 2021 ACD); Docket No. ACR2020, *Annual Compliance Determination*, March 29, 2021, at 91-95 (FY 2020 ACD). See also Docket No. ACR2019, *Annual Compliance Determination*, March 25, 2020, at 86-89 (FY 2019 ACD); Docket No. ACR2018, *Annual Compliance Determination*, April 12, 2019, at 112-17 (FY 2018 ACD).

recovery of both product- and group-level attributable costs for Competitive products collectively. *Id.* at 25-33. This is because incremental costs¹⁹ currently form the basis for both cost attribution and testing for cross-subsidization of Competitive products by Market Dominant products. *Id.* at 5-6. Therefore, the price floor under 39 U.S.C. § 3633(a)(1) is currently equivalent to the total attributable cost of Competitive products collectively, which includes both individual product-level incremental costs as well as group-level costs that are incremental for Competitive products collectively. *Id.* at 6.

The Commission next discussed the regulatory scheme for Competitive products and articulated the Commission's interpretation of 39 U.S.C. § 3633(a)(3) and (b). *Id.* at 40-71. Based on the PAEA's text, context, and structure, as confirmed by its history, the Commission found that the purpose of the appropriate share provision is to ensure fair competition in the market for competitive postal services by protecting against any possibility that prices for the Postal Service's Competitive products (despite covering their attributable costs), might nevertheless be anticompetitive as a result of the Postal Service's institutional costs being jointly incurred by both Market Dominant and Competitive products. *Id.* at 62.

The Commission concluded that the primary focus of the appropriate share provision is on protecting competition, rather than ensuring a particular level of institutional cost coverage. *Id.* Thus, the PAEA requires the Commission to periodically review the appropriate share requirement and expressly grants the Commission the authority to eliminate the appropriate share requirement, if warranted by the Commission's review. *Id.* The PAEA expressly confers broad authority on and discretion to the Commission to determine whether to retain the appropriate share

¹⁹ Incremental costs are the variable and fixed costs that would be eliminated if a product or group of products were discontinued, or, equivalently, the total cost caused by the product or group of products. See *id.* at 25-27. Notably, incremental costs are sub-additive, meaning that, due to scale and scope economies, the calculation of the incremental cost of Competitive products collectively will be greater than the sum of the incremental costs calculated for each separate Competitive product individually. *Id.* at 29-30.

requirement, and if so, to set the minimum contribution level, subject to considering all relevant circumstances, pursuant to 39 U.S.C. § 3633(b). *Id.* at 56-57. Likewise, 39 U.S.C. § 3633(b) confers broad authority and discretion to the Commission, when conducting its periodic reviews of the appropriate share requirement, to determine what circumstances are relevant, as well as how much weight to place on any particular circumstance. *Id.*

Considering the issues identified by the court, the Commission clarified that the “uniquely or disproportionately associated” phrase appearing in 39 U.S.C. § 3633(b) is broader than the “reliably identified causal relationship” standard for cost attribution under 39 U.S.C. § 3631(b), such that the latter can be viewed as a subset of the former. *Id.* at 52-53. The Commission also, as directed on remand, considered the “uniquely or disproportionately associated” phrase as applied to all accrued costs, including both attributable and institutional costs. *Id.* at 54-55. At the same time, the Commission found that where the “uniquely or disproportionately associated” phrase overlaps with the “reliably identified causal relationships” standard, the Commission has discretion to determine, using its expert judgment, the weight to assign such costs in determining the appropriate share. *Id.* at 55-56. The legislative history does not indicate that Congress intended for the Commission to account for such costs more than once in setting the price floor under 39 U.S.C. § 3633(a)(3). *Id.* at 70.

The Commission also found that 39 U.S.C. § 3633’s text, which requires the Commission to “consider *all relevant* circumstances, including . . . *the degree to which* any costs are uniquely or disproportionately associated with any competitive products,” confers discretion upon the Commission regarding how to fill in any gaps with respect to relevance and the degree of relationship at issue. *Id.* at 54; see 39 U.S.C. § 3633(b) (emphasis added).

After applying its interpretation of 39 U.S.C. § 3633(a)(3) and (b) to “all relevant circumstances,” the Commission elected to maintain the dynamic formula-based

approach to determining the appropriate share. Order No. 6043 at 71-109. The Commission found that under 39 U.S.C. § 3633(a)(3), the prices set for Competitive products must be marked up sufficiently to generate revenue above and beyond the costs attributable to Competitive products at the individual product and group level to also cover an appropriate share of the Postal Service's institutional costs. *Id.* at 74-80. Thus, in operation, the Commission's calculation of the price floor under 39 U.S.C. § 3633(a)(3) already includes the price floor calculated pursuant to 39 U.S.C. § 3633(a)(1). *Id.* at 8. The price floor set by 39 U.S.C. § 3633(a)(3) is made up of the appropriate share of institutional costs, as determined by the Commission, plus the attributable cost of Competitive products collectively. *Id.* As a result, the price floor set by 39 U.S.C. § 3633(a)(3) is higher than both price floors set by 39 U.S.C. § 3633(a)(1) and (a)(2). *Id.*

Because the Commission found that all attributable costs are already included in the Competitive product price floor under 39 U.S.C. § 3633(a)(3), the Commission declined to further account for them as part of the appropriate share. *Id.* at 78-79. Double-counting such costs would be economically unsound and would undermine the Postal Service's ability to effectively compete. *Id.*

The Commission applied the "uniquely or disproportionately associated" phrase to all of the Postal Service's accrued costs, analyzing the degree to which any costs are "uniquely or disproportionately associated" with any products, consistent with the existing costing methodology. *Id.* at 72-97. Under that methodology, costs are generally grouped by the activity for which they are incurred, and then distributed to products based on the proportion of that activity associated with each product. *Id.* at 74. The Commission found that there are presently no costs (other than those that also meet the definition of attributable costs) that can be identified to be "uniquely or disproportionately associated with any competitive products." *Id.* at 74-80; see 39 U.S.C. § 3633(b).

As directed on remand, the Commission specifically considered whether any institutional costs are “still related in some meaningful way to competitive products” See *UPS II*, 955 F.3d at 1045. The Commission found that formerly there were costs categorized as institutional costs that could have been linked to Competitive products, but, under the current cost attribution methodology, those costs are now categorized as attributable costs. Order No. 6043 at 8-9, 79-80. The nature of the residual costs which remain in the institutional cost category is such that the relationships between such costs and specific products or groups of products is not discernible or quantifiable. *Id.* at 9, 80-85.

The Commission found that while it is true theoretically that a portion of institutional costs is, in part, related to Competitive products, a portion is also, in part, related to Market Dominant products, and it is not possible to quantify the degree to which a particular institutional cost is associated with one or the other. *Id.* The Commission explained that the existence of such costs is inevitable for a multiproduct firm with large economies of scale and scope—economies derived from a joint processing and delivery network that simultaneously handles both Market Dominant and Competitive products. *Id.* at 9, 80-97. There is no method to identify a portion of institutional costs as associated with Competitive products that would not be arbitrary. *Id.* Moreover, employing arbitrary cost allocation methods would distort fair competition and seriously undermine the Postal Service’s ability to compete. *Id.* at 85-95. As a result, the Commission concluded that there is no meaningful relationship between Competitive products and any institutional costs, and hence there is no portion of institutional costs that are uniquely or disproportionately associated with any Competitive products. *Id.* at 84.

At the same time, the Commission found that the inability to further allocate institutional costs under the current costing methodology does not mean that the Postal Service has an unfair competitive advantage with respect to Competitive products. The

best available evidence suggests that the market is healthy and competitive. *Id.* at 97-109. No evidence indicates that the Postal Service has engaged in anticompetitive pricing of Competitive products; to the contrary, the evidence suggests that the Postal Service is incentivized to maximize Competitive product profits, and its market conduct has been in line with what would be expected of a profit-maximizing firm.²⁰ Competitive product contribution to institutional costs has always exceeded the required amount, often by a significant margin. Order No. 6043 at 93. At the same time, however, the Commission explained that it has elected to retain the appropriate share to serve as a margin of safety against any possibility of the Postal Service having an unfair competitive advantage, and that under the formula-based approach the appropriate share requirement would increase due to growth in the profitability or market share of the Postal Service's Competitive products. *Id.* at 94-95.

Having made these clarifications and findings, the Commission reissued its proposed rule to implement the dynamic formula-based approach. It again explained how the formula operates and how it accounts for the prevailing competitive conditions in the market and other relevant circumstances that the Commission historically considered qualitatively when evaluating the appropriate share requirement. *Id.* at 97-109. Because the dynamic formula-based approach reasonably reflects the qualitative statutory criteria from 39 U.S.C. § 3633(b), it easily falls within the Commission's broad discretion to determine what the appropriate share should be. *Id.* at 98-99. The Commission concluded that the appropriate share requirement, as derived from the formula, is sufficient to prevent the possibility of the Postal Service engaging in anticompetitive pricing of Competitive products. *Id.* at 103-05. The Commission also updated its market analysis to account for changes in the market for competitive postal services that had occurred since the remanded order (Order No. 4963) had been

²⁰ *Id.* at 104-05, n.153 (citing *id.* at 80-95; Order No. 4742 at 56-57; Order No. 4963 at 11-12) See also n.156, *infra*.

issued. *Id.* at 105-09. The Commission concluded that while the overall market had experienced significant growth because of the COVID-19 pandemic, the increase to the Postal Service's market share had been modest, and the dynamic formula-based approach had functioned as it was designed to, with the formula-based appropriate share having increased in response to these changes. *Id.*

Finally, the Commission addressed specific costs that UPS alleged were improperly excluded from the Commission's calculation of the appropriate share. *Id.* at 109-29. For each of these costs, the Commission explained why alterations to the Commission's dynamic formula-based approach were unreasonable. *Id.*

The Commission invited public comment on whether Order No. 6043 addressed the issues identified in *UPS II* adequately and whether the Commission should consider any additional costs in reviewing the appropriate share. *Id.* at 130-131. Additionally, the Commission invited commenters to propose alternative statutory interpretations and to identify any specific additional costs for the Commission to consider under any alternative statutory interpretation. *Id.*

C. Final Rule

In response to Order No. 6043, the Commission received and considered comments with respect to nearly every aspect of the Commission's findings in Order No. 6043 and the Commission's decision to readopt the dynamic formula-based approach to setting the appropriate share. In Section IV., *infra*, the Commission addresses comments relating to the Commission's statutory interpretation of the appropriate share provisions at 39 U.S.C. § 3633(a)(3) and (b). After considering these comments, the Commission has determined not to alter its interpretation as articulated in Order No. 6043, which the Commission continues to conclude is consistent with the PAEA's text and structure, as well as its context and legislative history. See Section IV., *infra*.

In Section V.A., *infra*, the Commission addresses comments relating to the application of the “uniquely or disproportionately associated” phrase from 39 U.S.C. § 3633(b) to the Postal Service’s accrued costs. The Commission continues to find that all attributable costs are already included in the 39 U.S.C. § 3633(a)(3) price floor and are furthermore implicitly considered as part of the formula. See Section V.A.2.b., *infra*. The price floors set under 39 U.S.C. § 3633(a)(1) and (a)(3) fully ameliorate any competitive deficit alleged to be unaddressed by the price floor under 39 U.S.C. § 3633(a)(2), and that the use of incremental costs for purposes of the price floors under 39 U.S.C. § 3633(a)(1) and (a)(2) is sufficient to prevent subsidization of Competitive products. See Section V.A.3.b., *infra*. Any further attempt to account for attributable costs as part of the appropriate share would constitute double-counting of those costs that would be economically unsound and potentially harmful to the Postal Service. See Section V.A.4.b., *infra*. There is no meaningful relationship between unattributed inframarginal costs and Competitive products; there are no costs uniquely or disproportionately associated with Competitive products within currently-existing institutional costs; and using economically sound measurement is reasonable. See Sections V.A.5.b., V.A.6.b., V.A.7.b., *infra*. The arbitrary allocation of institutional costs to Competitive products would contravene the intent of the PAEA, would be economically unsound, would degrade the existing costing methodology, and could harm the Postal Service and consumers. See Section V.A.8.b., *infra*.

In Section V.B., *infra*, the Commission addresses comments relating to the prevailing competitive conditions in the market and other relevant circumstances. The Commission confirms that revenue is the appropriate measure of market size, and that the profitability of competitors is relevant to assessing the prevailing competitive conditions in the market. See Section V.B.2.b., *infra*. The Commission presents an updated market analysis and continues to find that the state of competition in the market for competitive postal services is healthy. See *id.*, *infra*.

With respect to comments suggesting that the Commission should consider the Postal Service's financial losses, the "non-existence of a level playing field" and "subsidization," the Commission explains why these three potential circumstances are not relevant to this review. See Section V.B.3.b., *infra*. The Commission finds that comparative harm and the balance of risk and actual Competitive product contribution to institutional costs are relevant circumstances which all weigh in favor of readopting the dynamic formula-based approach. See *id.*, *infra*. Finally, the Commission reiterates its dismissal of comments alleging that the formula is arbitrary and capricious. See Section V.B.4.b., *infra*.

In Section VI., *infra*, the Commission addresses comments regarding the Commission's analysis pursuant to uncodified section 703(d) of the PAEA. See PAEA § 703(d). In accordance with that provision, the Commission invited additional public comment regarding Commission updates to a quantification by the Federal Trade Commission (FTC) of the net economic effect of federal and state laws that apply differently to the Postal Service than to private competitors in the market for competitive postal services, based on subsequent events that the Commission found affected the ongoing validity of the FTC's findings. See Order No. 6269. The Commission concludes that the additional events (beyond those identified by the Commission in Order No. 6269) raised by commenters are outside the scope of the Commission's 703(d) analysis. See Section VI.C., *infra*.

In Section VII., *infra*, the Commission addresses arguments relating to each specific type of costs alleged by any commenters to be uniquely or disproportionately associated with Competitive products. Upon consideration of each category of costs raised, the Commission concludes that none of these costs raised by commenters are uniquely or disproportionately associated with Competitive products and that it would be inappropriate to alter the formula-based approach to take these cost categories into account. See Section VII., *infra*.

In Section VIII., *infra*, the Commission addresses comments proposing alternatives to the formula-based approach to setting the appropriate share. The Commission concludes that UPS's four alternative proposals would each involve the arbitrary allocation of institutional costs to Competitive products, and furthermore all suffer from numerous methodological flaws and inconsistencies with the PAEA. See Sections VIII.A.3., VIII.B.3., VIII.C.3., VIII.D.3., *infra*. With respect to comments that the appropriate share should be eliminated, the Commission reiterates that it has, pursuant to the discretion accorded to it by 39 U.S.C. § 3633(b), elected to retain the appropriate share requirement as a margin of safety against any possibility of the Postal Service having an unfair competitive advantage. See Section VIII.E.3., *infra*.

IV. STATUTORY INTERPRETATION OF 39 U.S.C. CHAPTER 36

A. Background

As directed on remand, Order No. 6043 articulated the Commission's interpretation of 39 U.S.C. § 3633(a)(3) and (b) and how those provisions interact with the rest of the PAEA, including 39 U.S.C. § 3633(a)(1) and (a)(2) and the "reliably identified causal relationships" standard for cost attribution under 39 U.S.C. § 3631(b). Order No. 6043 at 40-71. Pursuant to *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.* ("*Chevron*"), 467 U.S. 837 (1984), the Commission "exhaust[ed] the traditional tools of statutory construction to determine whether Congress has spoken to the precise question at issue[,] . . . [which] include an examination of the statute's text, legislative history, and structure, as well as its purpose."²¹ The Commission "consider[ed] not only the language of the particular statutory provision under scrutiny,

²¹ *Petit v. U.S. Dep't of Educ.*, 675 F.3d 769, 781 (D.C. Cir. 2012) (quoting *Bell Atl. Tel. Cos. v. FCC*, 131 F.3d 1044, 1047 (D.C. Cir. 1997) (internal marks and citation omitted)).

but also the structure and context of the statutory scheme of which it is a part.”²² The Commission explained how its interpretation of 39 U.S.C. § 3633(a)(3) and (b) was consistent with the plain text, structure, and purpose of 39 U.S.C. § 3633 and of the PAEA more generally, and would therefore survive judicial scrutiny under *Chevron* step one. Order No. 6043 at 43-63. In the alternative, the Commission explained how even if 39 U.S.C. § 3633(a)(3) and (b) were to be construed as ambiguous, the Commission’s interpretation of those provisions is based on a permissible construction of the PAEA and would therefore be entitled to deference under *Chevron* step two.²³

The Commission began its interpretation with 39 U.S.C. § 3633’s text and structure. The statutory provisions setting forth the regulatory scheme for the Postal Service’s Competitive products appear in subchapter II of 39 U.S.C. chapter 36. Order No. 6043 at 41. Generally, 39 U.S.C. § 3632(a) authorizes the Governors of the Postal Service to establish rates for Competitive products, subject to regulations promulgated by the Commission pursuant to 39 U.S.C. § 3633. Specifically, 39 U.S.C. § 3633(a) requires the Commission to promulgate regulations necessary to “prohibit the subsidization of competitive products by market-dominant products[;]” 39 U.S.C. § 3633(a)(1); “ensure that each competitive product covers its costs attributable[;]” 39 U.S.C. § 3633(a)(2); and “ensure that all competitive products collectively cover what the Commission determines to be an appropriate share of the institutional costs of the Postal Service.” 39 U.S.C. § 3633(a)(3). “Costs attributable” is defined as “the direct

²² *Petit*, 675 F.3d at 781-82 (quoting *Cnty. of Los Angeles v. Shalala*, 192 F.3d 1005, 1014 (D.C. Cir. 1999) (internal marks and citation omitted)).

²³ Order No. 6043 at 63-71. An agency may argue in the alternative as to whether its reading of a statute is proper under *Chevron* step one or *Chevron* step two. See, e.g., *UPS I*, 890 F.3d at 1063 (“Given our conclusion that the Commission’s reading of ‘institutional costs’ is reasonable and so merits our deference [under *Chevron* step two], we need not consider the Commission’s argument that, under *Chevron* [step one], its reading is not only permissible, but also unambiguously correct.”); *Decatur Cty. Gen. Hosp. v. Johnson*, 602 F. Supp. 2d 176, 186 n.6 (D.D.C. 2009) (holding that agency’s decision to apply cost reduction factors to base year costs was entitled to deference under *Chevron* step two, where the agency also provided an alternative justification under *Chevron* step one).

and indirect postal costs attributable to . . . product[s] through reliably identified causal relationships.” 39 U.S.C. § 3631(b). Additionally, 39 U.S.C. § 3633(b) provides:

Five years after the date of enactment of this section, and every 5 years thereafter, the Postal Regulatory Commission shall conduct a review to determine whether the institutional costs contribution requirement under subsection (a)(3) should be retained in its current form, modified, or eliminated. In making its determination, the Commission shall consider all relevant circumstances, including the prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products.

39 U.S.C. § 3633(b).

Unlike the price floors required by 39 U.S.C. § 3633(a)(1) and (a)(2), the price floor under 39 U.S.C. § 3633(a)(3) is not necessarily a permanent component of Competitive product regulation. Order No. 6043 at 49, 59-60. Instead, 39 U.S.C. § 3633(b) explicitly grants the Commission the authority to eliminate the appropriate share requirement imposed on Competitive products collectively if the Commission determines that the relevant circumstances, including “the prevailing competitive conditions in the market” and “the degree to which any costs are uniquely or disproportionately associated with any competitive products,” warrant elimination. *Id.* Moreover, the appropriate share requirement constitutes a minimum, not a maximum, contribution level. *Id.* at 46-47. For these reasons, the Commission concluded that ensuring a particular level of institutional cost coverage by Competitive products is not the primary purpose of the appropriate share requirement. *Id.* at 62. Rather, the Commission interpreted the appropriate share requirement’s primary focus as being to ensure fair competition in the market in which Competitive products compete by protecting against any possibility that the Postal Service’s Competitive products could be anticompetitively priced, despite covering the costs required by the price floors under 39 U.S.C. § 3633(a)(1) and (a)(2). *Id.* The Commission’s interpretation—that the appropriate share requirement is focused on preventing and/or correcting the possibility

of a market imbalance arising as a result of the Postal Service's pricing decisions—is consistent with 39 U.S.C. § 3633(b)'s requirement that the Commission periodically review the appropriate share requirement (taking into account market considerations) so that the Commission can periodically reassess whether and to what extent such a margin of safety is necessary to protect competition. *Id.* at 62.

Specifically with respect to the “uniquely or disproportionately associated” phrase in 39 U.S.C. § 3633(b), while the Commission must “consider” all “relevant” circumstances, including “the degree to which” any costs are uniquely or disproportionately associated with any Competitive products, the statute does not prescribe the weight that the Commission must give to such considerations. *Id.* at 51. Instead, the statute authorizes the Commission to make determinations as to the relevance and the degree of relationship based on the Commission's expertise in postal costing, economics, and policy. *Id.* at 50-51.

Consistent with the court's instruction in *UPS II*, the Commission clarified that the scope of costs encompassed by the phrase “uniquely or disproportionately associated” in 39 U.S.C. § 3633(b) is broader than the scope of costs encompassed by the phrase “reliably identified causal relationships” in 39 U.S.C. § 3631(b). *Id.* at 52-53 (citing *UPS II*, 955 F.3d at 1049-50). However, the two phrases overlap in the sense that a cost meeting the definition of being “uniquely or disproportionately associated” with a product or group of products could also meet the narrower definition of exhibiting a “reliably identified causal relationship” with that product or group of products. *Id.* at 53. The Commission found that 39 U.S.C. § 3633(b) leaves to the Commission's discretion, based on its expert judgment, the question of what weight to assign such costs in determining what the appropriate share should be. *Id.* Given the interrelationship of the price floors under 39 U.S.C. § 3633(a) and the overlap between the “uniquely or disproportionately associated” and “reliably identified causal relationship” phrases, the Commission declined to account for costs more than once (*i.e.*, double count) in the

calculation of the price floor set by 39 U.S.C. § 3633(a)(3), which the Commission found would be economically unsound and harmful to the Postal Service's Competitive business. *Id.* at 55-56.

Based on the plain language of the “uniquely or disproportionately associated” phrase in 39 U.S.C. § 3633(b), a cost is “uniquely associated” with Competitive products if the cost is distinctly related or connected with a Competitive product or products, while a cost is “disproportionately associated” with Competitive products if the cost's relationship with a Competitive product or products is out of proportion relative to the cost's relationship to other products or groups of products. *Id.* at 51-52. Having clarified the foregoing, the Commission concluded that readoption of the dynamic formula-based approach to calculating the appropriate share was both expressly permissible and reasonable under the broad discretion conferred by the statute. *See id.* at 56, 64. This course of action was entirely consistent with the express opinion of the court, which recognized “that the Commission might decide against revising its bottom-line judgment [to readopt a dynamic formula-based approach to calculating the appropriate share], given the other factors the Commission must consider under § 3633(b) and the latitude that the text affords the Commission in making a final determination.”²⁴

After explaining its approach to the statutory construction, the Commission specifically invited commenters to put forth alternative statutory interpretations. *See* Order No. 6043 at 130. Commenters raised the following issues: whether the appropriate share provision's primary purpose is directed at cost allocation; whether the appropriate share provision's primary purpose is directed at preventing subsidization;

²⁴ *UPS II*, 955 F.3d at 1051. An agency may adhere to the same result on remand; judicial “review is still a matter of determining whether the agency's final decision ‘was based on a consideration of the relevant factors and whether there has been a clear error of judgment.’” *City of Los Angeles*, 165 F.3d at 978 (quoting *Competitive Enter. Inst. v. Nat'l Highway Traffic Safety Admin.*, 45 F.3d 481, 484 (D.C.Cir.1995) (quoting *Motor Vehicle Mfrs. Ass'n, Inc. v. State Farm Mutual Auto. Ins. Co.*, 463 U.S. 29, 43 (1983))).

whether 39 U.S.C. § 3622(b) is relevant to the Commission's review of the appropriate share requirement; whether prior Commission statements foreclose the Commission from readopting the dynamic formula-based approach to setting the appropriate share; whether the Commission properly considered "the degree to which any costs are uniquely or disproportionately associated with any competitive products" pursuant to 39 U.S.C. § 3633(b); and whether the Commission properly investigated both institutional and attributable costs to determine if any are potentially "uniquely or disproportionately associated with any competitive products" pursuant to 39 U.S.C. § 3633(b).

B. Cost Allocation is Not the Appropriate Share Provision's Primary Purpose

1. Comments

Throughout this proceeding and on appeal, UPS has taken the view that the appropriate share requirement is primarily a mechanism for allocating institutional costs between Market Dominant and Competitive products to prevent what UPS refers to as "subsidization" in the form of the price floors for Competitive products not being set high enough to recover Competitive products' "share" of institutional costs. UPS Comments at 40; see UPS Brief at 2, 51.

The Postal Service and Pitney Bowes, Inc. (Pitney Bowes), on the other hand, argue that UPS's interpretation of the appropriate share requirement's purpose would blur the line between costing and pricing by treating the allocation of institutional costs as an extension of the costing process, rather than as a circumstance to be considered as part of the pricing process. Postal Service Reply Comments at 6-37; Pitney Bowes Reply Comments 3. The Postal Service asserts that UPS's interpretation would effectively create, in addition to attributable costs and institutional costs, a third category

of “associated” costs, based on extended inferences of causation.²⁵ The Postal Service avers that such an interpretation is contrary to both the plain language and the legislative history of the PAEA. *Id.* at 6-37. Moreover, the Postal Service disputes the notion that there exists such a thing as Competitive products’ “fair share” of institutional costs. *Id.* at 40-41. The Postal Service maintains that institutional costs, by definition, are costs that cannot be causally linked with either Market Dominant or Competitive products. *Id.* at 41. They are costs that “belong to the institution as a whole.” *Id.*

Amazon.com Services LLC (ASL) and the Public Representative argue that UPS’s interpretation of the appropriate share requirement’s purpose would, by mandating total recovery of institutional costs, have the effect of reimposing a break-

²⁵ Postal Service Reply Comments at 15-16:

UPS is . . . explicitly claiming that the ‘appropriate share’ provisions—sections 3633(a)(3) and 3633(b)—jointly introduce an intermediate third category of costs that do not meet the definition of costs attributable, yet . . . should not be treated as institutional and recovered through application of the discretionary pricing factors

id. at 16 n.11 (“[O]nce reclassified as ‘associated’ costs, costs that were previously classified as ‘institutional’ are no longer ‘institutional’ in any meaningful sense of the term Costs cannot be considered residual institutional costs . . . if they are included in a mandatory cost floor”)

id. at 19:

UPS . . . apparently presumes that Congress intended the ‘associated’ provision to require the Commission to first start with the cost floor created by Competitive products based on their reliably attributed costs, to next ‘go beyond’ this and re-examine the residual pool of institutional costs to determine if any can be identified as ‘associated’ with Competitive products using a looser standard and then, if any costs previously-designated as institutional can be so identified, to increase the appropriate share accordingly.

id.:

UPS would treat . . . the appropriate share evaluation not as a pricing exercise (how to, if necessary, provide guidance for setting rates for Competitive products above the required cost floor such that resulting portions of institutional costs covered by Competitive and Market Dominant products are appropriate), but rather merely as another bite at the costing exercise (pushing up the cost floor for rates by reclassifying costs otherwise treated as institutional. (emphasis in original).

even requirement. ASL Reply Comments at 9; PR Reply Comments at 6. ASL, Pitney Bowes, and the Public Representative assert that UPS treats the appropriate share as if it were a ceiling, as opposed to a floor.²⁶ ASL and Pitney Bowes argue that UPS's interpretation fails to adequately account for the prevailing competitive conditions in the market, the other explicit criterion from 39 U.S.C. § 3633(b). ASL Reply Comments at 10-11; Pitney Bowes Reply Comments at 9. The Postal Service, ASL, Dr. John C. Panzar, and Pitney Bowes all note that the Commission has the explicit authority under 39 U.S.C. § 3633(b) to eliminate the appropriate share, and as a result they argue that the requirement's optional nature is inconsistent with UPS's view that the appropriate share was intended to function primarily as a cost allocation provision.²⁷ ASL argues that "UPS seeks to re-litigate cost attribution issues that were not previously resolved in its favor[.]" and "UPS . . . urges the Commission to abandon economically sound costing methodologies in favor of any number of arbitrary, alternative price floors and costing models, all of which ultimately have some basis in the widely discredited approach of fully distributed costing." ASL Reply Comments at 4.

Dr. Panzar characterizes the appropriate share requirement as "an additional policy tool provided to the Commission for use during the transition between the cost of service regulation of the Postal Reorganization Act of 1970 (PRA) and the light-handed regulatory approach of the PAEA" Panzar Decl. at 6. He notes that "[g]iven that the purpose of section 3633 is to ensure fair competition, it is important to recognize that *competition*, (as opposed to *competitors*) can be harmed by an appropriate share requirement that is set too high." Panzar Reply Decl. at 5 (emphasis in original).

²⁶ ASL Reply Comments at 8; Pitney Bowes Reply Comments at 9; PR Reply Comments at 7-8.

²⁷ Postal Service Comments at 7-8; ASL Reply Comments at 4-5, 8-9; Panzar Decl. at 6; Pitney Bowes Reply Comments at 8.

2. Commission Analysis

The Commission begins with the statutory text, which requires that Competitive products cover an “appropriate share” of the Postal Service’s institutional costs. 39 U.S.C. § 3633(a)(3). The text of 39 U.S.C. § 3633(a)(3) does not say what share of institutional costs would be “appropriate.” Order No. 6043 at 46. To the contrary, Congress expressly provided at 39 U.S.C. § 3633(b) that the Commission may “retain[], modif[y], or eliminate[]” the appropriate share entirely, based on what the Commission determines to be “appropriate.” 39 U.S.C. § 3633(b). This express grant of discretion to the Commission is unambiguous and undermines the argument that the appropriate share provision must be interpreted as requiring something tantamount to fully distributed costing, which is a methodology that has been widely discredited by expert economists as economically unsound for use with respect to the Postal Service and would run counter to Congress’s express intent of ensuring accuracy in postal costing.²⁸

In determining what the appropriate share should be, the Commission must “*consider* all relevant circumstances, including the prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products.” 39 U.S.C. § 3633(b) (emphasis added). “Consider” means “to think about carefully,” or “to take into account—it is not prescriptive and does not mean that the Commission must “adhere to,” “be bound by,” or “follow” any particular relevant circumstance in reaching its determination.²⁹ The text of 39 U.S.C. § 3633(b) does not prescribe the weight that the Commission must give to any particular circumstance it deems to be relevant. Order No. 6043 at 51.

²⁸ Order No. 6043 at 85-91. The phrases “fully distributed costing” and “fully-allocated costing” are used interchangeably.

²⁹ Order No. 6043 at 50. See *United States v. Bruce*, 285 F.3d 69, 73 (D.C. Cir. 2002) (noting that statutory language requiring the court to “consider” the applicable guidelines or policy statements “does not mean to ‘adhere to,’ ‘be bound by’ or ‘follow’” those materials in imposing a sentence).

The first specifically enumerated relevant circumstance under 39 U.S.C. § 3633(b)—“the prevailing competitive conditions in the market”—is plainly focused on assessing the current state of competition in the market in which the Postal Service’s Competitive products compete. Order No. 6043 at 51. UPS’s interpretation of the appropriate share requirement’s purpose barely addresses this circumstance, and instead focuses solely on the second specifically enumerated relevant circumstance in 39 U.S.C. § 3633(b)—“the degree to which any costs are uniquely or disproportionately associated with any competitive products.” While the use of the words “any” and “associated” in this phrase connote broad applicability with respect to the potential scope of costs to be considered, the use of the words “the degree to which” connotes wide discretion on the Commission’s part as to the extent to which such costs must be reflected in the Commission’s determination as to what the appropriate share should be. Order No. 6043 at 52. The requirement that the Commission “consider” “the degree to which” any costs are uniquely or disproportionately associated with any Competitive products does not in any way mandate that the Commission accept the argument that the appropriate share provision should be interpreted as requiring something akin to fully distributed costing.

The structure of 39 U.S.C. § 3633 and of the PAEA more generally reinforce these conclusions. Section 3633 contains three components. First, it requires the Commission to prohibit the subsidization of Competitive products by Market Dominant products. 39 U.S.C. § 3633(a)(1). Second, it requires the Commission to ensure that each Competitive product covers its attributable costs. 39 U.S.C. § 3633(a)(2). Third, it requires the Commission to ensure that all Competitive products collectively cover what the Commission determines to be an appropriate share of the Postal Service’s institutional costs. 39 U.S.C. § 3633(a)(3). However, pursuant to 39 U.S.C. § 3633(b), the Commission must determine, starting 5 years after the PAEA’s enactment and again every 5 years thereafter, “whether the institutional costs contribution requirement under subsection (a)(3) should be retained in its current form, modified, or eliminated.” 39

U.S.C. § 3633(b). Hence, while the cross-subsidization and cost coverage provisions of 39 U.S.C. § 3633(a)(1) and (a)(2) are permanent features of Competitive product regulation by statutory mandate, the PAEA leaves the question of whether to retain, modify, or eliminate the institutional costs contribution requirement of 39 U.S.C. § 3633(a)(3) entirely to the sound discretion of the Commission. When crafting the statute, Congress could have limited the Commission's discretion over the institutional costs contribution requirement in any number of ways, but Congress chose not to do so.³⁰ UPS's efforts to impose limits on Commission discretion that are not found in the PAEA would alter, rather than interpret, the PAEA.³¹ It would be inconsistent with 39 U.S.C. § 3633(a)(3) and (b)'s broad language—which expressly contemplates the possibility of the appropriate share being “eliminated”—to interpret the institutional costs contribution requirement as mandating that the appropriate share be set at any specific level, much less at a level that would constitute fully distributed costing.³²

³⁰ See *Little Sisters of the Poor Saints Peter & Paul Home v. Pennsylvania*, 140 S. Ct. 2367, 2381 (2020) (citing *Ali v. Fed. Bureau of Prisons*, 552 U.S. 214, 227 (2008); *Rotkiske v. Klemm*, 140 S. Ct. 355, 361 (2019); *Husted v. A. Philip Randolph Inst.*, 138 S. Ct. 1833, 1845–1846 (2018)).

³¹ See *Little Sisters of the Poor Saints Peter & Paul Home*, 140 S. Ct. at 2381 (2020) (citing *Nichols v. United States*, 136 S. Ct. 1113, 1118 (2016); *Watt v. Energy Action Educ. Found.*, 454 U.S. 151, 168 (1981)).

³² Federal courts assume that Congress knows how to circumscribe agency discretion in the process of crafting a statute and if there is any ambiguity regarding an expansive grant of authority, “there is ‘a presumption that Congress . . . desired the agency (rather than the courts) to possess whatever degree of discretion the ambiguity allows.’” *Corbett v. Transp. Sec. Admin.*, 19 F.4th 478, 487 (D.C. Cir. 2021), *cert. denied sub nom. Corbett, Jonathan v. TSA*, No. 22-33, 2022 WL 16542124 (Oct. 31, 2022) (quoting *Smiley v. Citibank (S.D.)*, N.A., 517 U.S. 735, 740-41 (1996)).

Furthermore, 39 U.S.C. § 3633(b)'s heading—“[r]eview of *minimum* contribution”—and the PAEA's overall context illustrate that the appropriate share requirement was intended to function as a minimum contribution level.³³ This is inconsistent with UPS's interpretation of the appropriate share provision's purpose as being to ensure “total cost coverage.” UPS Comments at 9, 16, 36. Moreover, 39 U.S.C. § 3633(a)(1) requires the Commission to “prohibit the subsidization of competitive products by market-dominant products.” 39 U.S.C. § 3633(a)(1). It strains credulity to believe that Congress—having required the Commission to prohibit the subsidization of Competitive products by Market Dominant products under 39 U.S.C. § 3633(a)(1)—then sought through the discretionary language of the appropriate share requirement at 39 U.S.C. § 3633(a)(3) and (b) to mandate additional protection against subsidization. Effectively, UPS's interpretation would render 39 U.S.C. § 3633(a)(1) superfluous.³⁴

³³ 39 U.S.C. § 3633(b) (emphasis added). See Order No. 6043 at 46-47. Although section headings cannot limit the plain meaning of a statutory text, they supply cues to what Congress intended. See *Merit Mgmt. Grp., LP v. FTI Consulting, Inc.*, 138 S. Ct. 883, 893 (2018) (citing *Florida Dep't of Revenue v. Piccadilly Cafeterias, Inc.*, 554 U.S. 33, 47 (2008); *Yates v. United States*, 135 S. Ct. 1074, 1083 (2015)). See also 2A Norman Singer and Shambie Singer, *Sutherland Statutory Construction* § 47:14 (7th ed. 2020).

³⁴ *Nat'l Postal Pol'y Council v. Postal Regul. Comm'n*, 17 F.4th 1184, 1191 (D.C. Cir. 2021), *cert. denied*, 142 S. Ct. 2868 (2022) (canon against surplusage) (citing *Mail Ord. Ass'n of Am. v. U.S. Postal Serv.*, 986 F.2d 509, 515 (D.C. Cir. 1993) (same)).

The history and purposes of the PAEA reinforce the foregoing conclusions. The PAEA's legislative history shows that for Competitive products, Congress's goal was to provide the Postal Service with greater pricing flexibility, subject to minimal Commission oversight to ensure fair competition.³⁵ Although prior versions of postal reform legislation introduced in the Senate would have required Competitive products to make a "reasonable contribution" to, or to cover "their share" of, institutional costs, the compromise language enacted in the final version of the PAEA was less prescriptive, requiring only that Competitive products contribute an "appropriate share" to institutional costs.³⁶ This language shows that the purpose of the appropriate share requirement was not simply to ensure a particular level of institutional cost coverage, which is what the Senate version of postal reform would have accomplished by requiring Competitive products to recover "their share" of institutional costs, but rather to ensure fair competition. Order No. 6043 at 69-70. Moreover, throughout the entire modern history of postal costing, Congress, the courts, and the Commission have uniformly rejected the

³⁵ Order No. 6043 at 65-66. See S. Rep. No. 108-318, 108th Cong. (2004), at 7 ("[T]he Postal Service's Board of Governors is permitted to more directly manage and price the Postal Service's competitive products; subject to minimal Regulatory Commission oversight to ensure that the Postal Service competes fairly with the private sector delivery services."); *Id.* at 14 ("This bill establishes a flexible system of pricing the Postal Service's competitive products which reduces the regulatory burdens and permits more customer- and market-responsive pricing. It does this while establishing appropriate safeguards to ensure that a level playing field is maintained and that the Postal Service does not unfairly compete."); H.R. Rep. No. 109-66, 109th Cong., pt. 1 (2005), at 44 ("[T]he Postal Service will compete on a level playing field, under many of the same terms and conditions faced by its private sector competitors, albeit with stronger controls, oversight, and limitations in recognition of its governmental status.").

³⁶ Order No. 6043 at 68-69. See, e.g., H.R. 4341, 108th Cong. (2004), H.R. Rep. No. 108-672, 108th Cong., pt. 1, at 86 (Sept. 8, 2004) (proposing to codify 39 U.S.C. § 3633(3) "to ensure that all competitive products collectively make a reasonable contribution to the institutional costs of the Postal Service."); H.R. 22, 151 Cong. Rec. H6524 (daily ed. Jul. 26, 2005) (proposing the same text to the 109th Congress); S. 2468, 150 Cong. Rec. S5990, 108th Cong. (daily ed. May 20, 2004) (proposing to codify 39 U.S.C. § 3633(3) to "ensure that all competitive products collectively cover their share of the institutional costs of the Postal Service"); S. 662, 152 Cong. Rec. S914 (daily ed. Feb. 9, 2006) (proposing the same text to the 109th Congress to be codified as 39 U.S.C. § 3633(a)(3)).

idea that postal rates ought to be set using fully distributed costing.³⁷ Therefore, UPS's arguments with respect to the appropriate share requirement's purpose are inconsistent with Congress's expressed intent.

While the Commission agrees with UPS that the purpose of the appropriate share requirement is to ensure fair competition in the market for competitive postal services, the Commission disagrees with UPS about how to achieve that purpose consistent with the goals encapsulated within the PAEA's statutory scheme. UPS views the appropriate share requirement primarily as a cost allocation provision, analogous to 39 U.S.C. § 3633(a)(1) and (a)(2). In the same way that 39 U.S.C. § 3633(a)(1) and (a)(2) ensure that Competitive product prices must cover all the costs that they cause, UPS views the purpose of the appropriate share requirement as mandating that the price floor for Competitive products is set high enough to cover some specific percentage of the Postal Service's institutional costs that, in UPS's view, represents their "fair share." See UPS Comments at 40. This proposed approach may be

³⁷ See, e.g., *Nat'l Ass'n of Greeting Card Publishers v. U.S. Postal Serv.*, 462 U.S. 810, 833 (1983) (specifically rejecting the imposition of an intermediary tier of costs, based on extended inferences of causation, between attributable and institutional costs). Congress in enacting the PAEA adopted the two-tier approach to cost attribution (classifying all costs as either attributable or institutional) that had been developed by the Postal Rate Commission under the PRA, and Congress explicitly codified "reliably identified causal relationships" as the standard for cost attribution. See Pub. L. 109-435, 120 Stat. 3201, 3205, §§ 3622(c)(2), 3631(b) (explicitly codifying "reliably identified causal relationships" as the standard for cost attribution) See also S. Rep. No. 108-318, at 9-10.

Over the history of the Postal Reorganization Act the ability to accurately attribute costs has continually evolved, and the Committee expects that . . . this process will continue. The current analysis has been guided by a Supreme Court decision, *National Assoc. of Greeting Card Publishers v. USPS*, 462 U.S. 810, 829-34, (1982), that carefully analyzed how the term attributable should be interpreted. This definition has been further refined by U.S. Courts of Appeals and is well understood in the industry. The NAGCP Court rejected a contention that it was appropriate to make classes responsible for the recovery of costs for which an extended inference of causation was claimed. It emphasized the need for reliable indicators of causality without specifying any specific method for identifying causality The Committee finds no reason for changing this standard.

intuitively appealing but accepting this approach would require the Commission to ignore important aspects of 39 U.S.C. § 3633's text and the PAEA's overall regulatory scheme and adopt an approach that would suffer from all the flaws of and harms flowing from fully distributed costing.

The Postal Service persuasively explains that UPS distorts the fundamental paradigm for the Commission's review of the appropriate share. UPS wrongly tries to allocate institutional costs by employing a less-economically rigorous extension of the costing process. Postal Service Reply Comments at 6-37. However, at its core, the Commission's appropriate share review is a discretionary pricing review, considering qualitative statutory criteria, rather than a costing exercise. This is illustrated by comparing the text of the appropriate share related provisions appearing in 39 U.S.C. § 3633(a)(3) and (b), with the cost coverage requirements appearing in 39 U.S.C. § 3633(a)(1) and (a)(2). The PAEA commands the Commission to periodically reevaluate if an appropriate share requirement is necessary at all (and if, so at what level). 39 U.S.C. § 3633(b). By contrast, the PAEA does not allow the Commission to eliminate the cost coverage requirements appearing in 39 U.S.C. § 3633(a)(1) and (a)(2); nor does the PAEA require periodic review of those requirements. Order No. 6043 at 49. The argument that the primary purpose of the appropriate share requirement is to ensure a particular level of institutional cost coverage by Competitive products is inconsistent with the statutory grant of authority to the Commission expressly contemplating potential elimination of the appropriate share requirement upon each periodic review.

UPS's interpretation also ignores other important aspects of 39 U.S.C. § 3633(b)'s text and structure. UPS's interpretation of the appropriate share requirement's purpose only focuses on the allocation of institutional costs to

Competitive products.³⁸ But 39 U.S.C. § 3633(b) is not solely limited to considering the degree to which any *institutional* costs are uniquely or disproportionately associated with any Competitive products—it requires the Commission to consider the degree to which *any* costs are uniquely or disproportionately associated with any Competitive products. See *UPS II*, 955 F.3d at 1050. UPS’s interpretation does not address either the possibility or the implications of attributable costs being uniquely or disproportionately associated with Competitive products.

UPS’s interpretation does not address the role that the other enumerated relevant circumstance in 39 U.S.C. § 3633(b)—the “prevailing competitive conditions in the market”—plays with respect to the appropriate share requirement’s purpose. As the Postal Service asserts, if the primary purpose of the appropriate share requirement were simply to allocate a “fair” portion of institutional costs to Competitive products, then it is unclear what role the state of competition in the market for competitive postal services plays in the analysis. Postal Service Reply Comments at 56.

The “degree to which any costs are uniquely or disproportionately associated with any competitive products” is just one of two non-exclusive relevant circumstances that the Commission must “consider” when reviewing the appropriate share requirement to determine what, if any, minimum contribution level is “appropriate.” Order No. 6043 at 50; Postal Service Reply Comments at 25-26. As the Commission explained in Order No. 6043, “consider” does not mandate any particular action by the Commission. Order No. 6043 at 50. By contrast, 39 U.S.C. § 3633(a)(1) and (a)(2) require more than “consideration” of relevant circumstances as part of a discretionary determination as to what amount is “appropriate”—they affirmatively require the Commission to “prohibit the subsidization of competitive products by market-dominant products” and “ensure that

³⁸ See Postal Service Reply Comments at 21 (citing Reply Brief for Petitioner United Parcel Service, Inc., at 8, *UPS II*, No. 19-1026, ECF Document No. 1814772, finalized November 7, 2019 (UPS Reply Brief)). See also UPS Brief at 19.

each competitive product covers its costs attributable.” *Compare* 39 U.S.C. § 3633(a)(1) and (a)(2), *with* 39 U.S.C. § 3633(b).

Nor does the word “consider” represent the only grant of discretion to the Commission in the second sentence of 39 U.S.C. § 3633(b). The Commission must consider all “relevant” circumstances, including “the degree to which any costs are uniquely or disproportionately associated with any competitive products,” but the statute does not prescribe the relative weight that the Commission must give to any particular circumstance it deems to be relevant. Order No. 6043 at 51. Further, the Commission must consider “*the degree to which* any costs are uniquely or disproportionately associated with any competitive products.” 39 U.S.C. § 3633(b) (emphasis added). This language provides wide discretion to the Commission as to the extent to which any such costs are relevant to the Commission’s appropriate share determination. Order No. 6043 at 52. Conversely, 39 U.S.C. § 3633(a)(1) and (a)(2) do not provide the Commission with this level of discretion.

The “uniquely or disproportionately associated” phrase does not appear in 39 U.S.C. § 3633(a)(3), but rather in 39 U.S.C. § 3633(b). And, as the Postal Service notes, the considerations appearing in 39 U.S.C. § 3633(b) did not become applicable until 5 years after the PAEA was enacted, at the time of the Commission’s first required review of whether to retain, modify, or eliminate the appropriate share requirement. Postal Service Reply Comments at 26-27. This undermines the argument that the appropriate share requirement’s primary purpose is implicitly contained in the “uniquely or disproportionately associated” phrase in 39 U.S.C. § 3633(b). *See id.* If the “uniquely or disproportionately associated” phrase carries the level of import assigned to it by UPS, the PAEA would not confer such a broad degree of discretion to the Commission to evaluate the degree to which the phrase may be a relevant consideration every 5 years, and would not explicitly allow the Commission to dismiss the phrase’s relevance entirely by eliminating the appropriate share requirement.

The Postal Service also correctly notes a lack of statutory parallelism between the “reliably identified causal relationships” standard for cost attribution at 39 U.S.C. § 3631(b) and the “uniquely or disproportionately associated” phrase from 39 U.S.C. § 3633(b). Postal Service Reply Comments at 24. This undermines the argument that the “uniquely or disproportionately associated” phrase is intended to function as a costing standard analogous to the “reliably identified causal relationships” standard. *Id.* Specifically, while the PAEA expressly defines “attributable costs” using the “reliably identified causal relationships” standard at both 39 U.S.C. § 3631(b) (with respect to Competitive products) and at 39 U.S.C. § 3622(c)(2) (with respect to Market Dominant products), the statute does not provide any express parallel definition for “uniquely or disproportionately associated” costs aside from its plain language. *Id.* 24-25. In addition, while the “reliably identified causal relationships” standard for cost attribution is codified at both 39 U.S.C. § 3631(b) (with respect to Competitive products) and at 39 U.S.C. § 3622(c)(2) (with respect to Market Dominant products), and while the appropriate share provision at 39 U.S.C. § 3633(a)(3) is likewise matched with respect to the Market Dominant ratemaking system at 39 U.S.C. § 3622(b)(9), there is no equivalent parallel Market Dominant reference to “uniquely or disproportionately associated” costs. *Id.* If Congress had intended for the “uniquely or disproportionately associated” phrase to function as a costing standard, then it might be expected that the PAEA would have treated the “uniquely or disproportionately associated” phrase equivalently to how the PAEA treated the “reliably identified causal relationships” standard, by statutorily defining the term and codifying it with respect to both Competitive products and Market Dominant products. Embedding “the degree to which any costs are uniquely or disproportionately associated with any competitive products” within the list of non-exclusive relevant considerations for the Commission to consider when periodically reviewing the appropriate share requirement under 39 U.S.C. § 3633(b) does not dictate the level of primacy that UPS assigns to the selected four words in the longer phrase of the text.

In addition to being inconsistent with 39 U.S.C. § 3633's text, UPS's interpretation of the appropriate share requirement's purpose is inconsistent with the PAEA's broader structure with respect to ratemaking. UPS's interpretation of the appropriate share requirement's purpose is inconsistent with the two-tier framework that has formed the basis for postal ratemaking since the 1970s, and which Congress explicitly adopted when it enacted the PAEA. See Postal Service Reply Comments at 16. Under that framework, the Postal Service first identifies all costs that can be reliably linked to individual products or groups of products, using Commission-approved costing methodologies, and attributes those costs to the products or product groupings. Order No. 6043 at 12. All remaining costs are classified as institutional, and are allocated across products via the pricing process, in which the attributable cost floors established in the costing tier are further marked up to recover institutional costs. *Id.* at 12-13.

In implementing the PRA, the former Postal Rate Commission developed the two-tier approach to costing.³⁹ That approach was upheld by the Supreme Court in *Nat'l Ass'n of Greeting Card Publishers* 462 U.S. at 833. In that case, the Supreme Court specifically rejected the imposition of an intermediary tier of costs, based on extended inferences of causation, between attributable and institutional costs. See *Nat'l Ass'n of Greeting Card Publishers*, 462 U.S. at 821-25. As the Postal Service argues, "[p]rofessing to identify a subset of associated costs within the set of non-attributable costs necessarily reduces the residual amount left to be allocated through the pricing process, and the result is unambiguously three tiers of costs" Postal Service Reply Comments at 28. During the PRA era, the allocation of institutional costs via markups took place as part of the rate-setting process, with the former Postal Rate Commission setting markups guided by statutory pricing factors that reflected the policy goals of the PRA. Order No. 6043 at 15, 34. The ratemaking regime under the PRA was a break-even system, in which rates were set so that the Postal Service (as a whole)

³⁹ Postal Reorganization Act, Pub. L. No. 91-375, 84 Stat. 719 (1970) (PRA).

would cover all its accrued costs (*i.e.*, both attributable and institutional costs). *Id.* at 16, 34.

Generally, the PAEA carried forward principles of costing from the PRA era. See *id.* at 24. Congress chose to maintain an integrated processing and delivery network for both Market Dominant and Competitive products.⁴⁰ Additionally, Congress adopted the two-tier approach to postal ratemaking that had been developed by the Postal Rate Commission under the PRA, and Congress explicitly codified “reliably identified causal relationships” as the standard for cost attribution in the PAEA. See n.37, *supra*. Pursuant to 39 U.S.C. § 3633(a)(1) and (a)(2), the Commission continues to refine and expand the costing methodologies established under the PRA to identify, measure, and allocate attributable costs, in which costs are attributed to products or groups of products on a causal basis to the maximum extent possible.⁴¹

The PAEA changed the treatment of institutional costs in significant ways compared to the former PRA. Order No. 6043 at 34. Under the PRA, the Postal Rate Commission did not allocate institutional costs based on any connection between those costs and particular products. *Id.* Instead, the markups that determined how much of the institutional costs were to be recovered by each product were selected by the Postal Rate Commission in accordance with pricing factors that reflected the policy goals of the

⁴⁰ See Pitney Bowes Reply Comments at 10-11 (“Congress has repeatedly affirmed its intent that the Postal Service operate an integrated network for the delivery of mail and packages together to enable the Postal Service to realize scale and scope economies that enhance its efficiencies.”). The principle of an integrated delivery network was explicitly endorsed in the Postal Service Reform Act of 2022 (PSRA), Pub. L. 117-108, § 202(a), 136 Stat. 1127, 1147 (“The Postal Service shall maintain an integrated network for the delivery of market-dominant and competitive products . . .”). An uncoded rule of construction was included in the notes of 39 U.S.C.A. 101 for this provision stating that “[n]othing in subsection [202](a) or the amendment made by such subsection is intended to alter or amend the requirements of chapters 20 or 36 of title 39, United States Code, and related implementing regulations, including provisions relating to costing, accounting, or rates.” PSRA § 202(b). Thus, the amendments appearing in PSRA § 202(a) do not alter the Commission’s decision in this proceeding.

⁴¹ Details concerning how postal costing developed under the PAEA, from the initial efforts to calculate incremental costs to the eventual expansion of cost attribution by the adoption of the incremental cost test appear in Order No. 6043. See Order No. 6043 at 22-33.

PRA, including the requirement that the Postal Service as a whole would cover all of its accrued costs and thus break even.⁴² Because the PRA required the Postal Rate Commission to recommend rates that would break even, these rates would collectively recover all of the institutional costs.⁴³

The PAEA, which was enacted in 2006, bifurcated Competitive products from Market Dominant products, removed the break-even restraint, and shifted rate-setting from the former Postal Rate Commission to the Governors of the Postal Service.⁴⁴ Under the PAEA, the Postal Service offers Competitive products in a competitive market where they compete against competitors' similar offerings. Order No. 6043 at 34. The bifurcation of Competitive products from Market Dominant products was intended to

⁴² See Order No. 6043 at 15, 34. After submission of suggestions by the Postal Service, former 39 U.S.C. § 3622(b) required the Postal Rate Commission to make a "recommended decision" in accordance with the policies of Title 39 and eight specific statutory factors. 39 U.S.C. § 3622(a) and (b) (2000) (amended 120 Stat. 3201). Former 39 U.S.C. § 3624(c) required that the Postal Rate Commission's recommended decision "include a statement specifically responsive to the criteria established under [former] section 3622" 39 U.S.C. § 3624(c) (2000) (repealed 120 Stat. 3217). For each rate suggested by the Postal Service, the Postal Rate Commission was obliged to exercise its best judgment as to which among a spectrum of lawful rates or classifications was the outcome most consistent with the PRA's criteria. In almost all cases, the Postal Rate Commission's decision was a final determination because the PRA provided little scope for change by the Governors under former 39 U.S.C. § 3625. 39 U.S.C. § 3625 (2000) (repealed 120 Stat. 3217).

⁴³ Order No. 6043 at 34. Formerly, the PRA imposed a break-even constraint on the Postal Service. 39 U.S.C. § 3621 (2000) (amended 120 Stat. 3200-01). Thus, the Postal Rate Commission's recommended rates and fees were designed to generate sufficient revenues to recover, as nearly as practicable, total estimated test year costs. See *id.*

⁴⁴ Order No. 6043 at 13, 15-16, 22. Under the bifurcated regulatory scheme established by the PAEA, products in the Market Dominant category are defined as all products covered by the postal monopoly as well as "each product in the sale of which the Postal Service exercises sufficient market power that it can effectively set the price of such product substantially above costs, raise prices significantly, decrease quality, or decrease output, without risk of losing a significant level of business to other firms offering similar products." 39 U.S.C. § 3642(b)(1)-(2). The postal monopoly is codified in the Private Express Statutes, which are a group of civil and criminal statutes that make it unlawful for any entity other than the Postal Service to send or carry letters. See 18 U.S.C. §§ 1693-1699; 39 U.S.C. §§ 601-606. Competitive products, by contrast, are defined as all other postal products that do not fall within the Market Dominant category. 39 U.S.C. § 3642(b)(1). While Competitive products consist largely of parcels, they also include express letters and flats and a wide variety of ancillary and non-postal products and services. See Mail Classification Schedule (MCS), part B, available at <https://www.prc.gov/mail-classification-schedule>.

allow for more flexible rate-setting by the Postal Service with respect to Competitive products, providing the Postal Service with the opportunity to price Competitive products in a way that maximizes their contribution to institutional costs. *Id.* at 13, 24.

The PAEA removed the break-even requirement, so it is permissible for rates to recover more than the total institutional costs. However, since the enactment of the PAEA, the constraints of the price cap on Market Dominant products, combined with competitive market conditions in the market in which Competitive products compete, have prevented the recovery of all institutional costs. *Id.* at 34. Because the PAEA permits the Postal Service to retain earnings from Competitive products, the Postal Service is expected and incentivized to maximize contribution from Competitive products by pricing Competitive products in line with similar products offered by competitors in order to compete effectively.⁴⁵ The role of Market Dominant products is to cover the remainder of the Postal Service's institutional costs not covered by Competitive products, to the extent that the revenue generated by Market Dominant products is able to do so. Order No. 6043 at 35.

⁴⁵ See Order No. 6043 at 34-35, 60-61 (citing Order No. 26 ¶ 3056; Order No. 4742 at 16; Order No. 4963 at 60-62).

After the PAEA's enactment, the Postal Regulatory Commission no longer focuses on setting rates with markups that allow the Postal Service to break even. *Id.* at 22, 34. Instead, the PAEA vests the Governors of the Postal Service with the authority to make the pricing decisions which determine the product revenues that go toward recovery of institutional costs, subject to the constraints of the Commission's regulation of Market Dominant and Competitive products.⁴⁶ As required by the regulatory scheme for Competitive products set forth under 39 U.S.C. § 3633, Competitive products must be priced high enough to cover the price floors under 39 U.S.C. § 3633(a)(1) and (a)(2), and the Commission-determined appropriate share under 39 U.S.C. § 3633(a)(3) and (b), but they must also be priced to compete effectively in the market for competitive postal services.⁴⁷ This is consistent with the PAEA's multi-faceted purpose with respect to the regulatory scheme for Competitive products. As a whole, 39 U.S.C. § 3633 focuses on Competitive product cost coverage so as to safeguard fair competition in the market for competitive postal services, while at the same time not unduly restraining competitive conduct in the market by the Postal Service. Order No. 6043 at 57.

⁴⁶ See *id.* at 34. As Dr. Panzar summarizes:

Congress enacted the PAEA to allow market forces to perform a greater role in promoting the fair and efficient operation of the postal sector. Because it is no longer subject to cost of service regulation and an overall "break even constraint," the Postal Service has every incentive to set the prices of its competitive services to maximize the contribution that those services make towards covering institutional costs. Consumers of competitive products are protected by the option to patronize the Postal Service's highly competitive rivals. Rivals are protected by the incremental cost price floor. Consumers of market dominant services are protected by the PAEA's price cap regulation.

Panzar Decl. at 4.

⁴⁷ Order No. 6043 at 23-24, 34. In contrast with the minimum requirements governing rate-setting of Competitive products under 39 U.S.C. § 3633 and the Commission's regulations, the PAEA and the Commission's regulations set a maximum (price cap) to govern rate-setting for Market Dominant products. See Order No. 6043 at 22-23.

Notably, while Congress in enacting the PAEA expressed its desire that cost attribution be expanded to the greatest extent technically feasible,⁴⁸ Congress was also clear that attribution should emphasize accuracy and be based on causality, and Congress noted the potential dangers associated with arbitrary cost distribution.⁴⁹ The

⁴⁸ S. Rep. No. 108-318, at 9 (“Identifying costs which can reliably be found to have been caused by each specific subclass and service is essential to maintaining economically efficient rates and avoiding inequitable cross-subsidization....”); *Id.* at 30 (“[T]he Postal Service and the Postal Regulatory Commission should partner with private sector accounting experts and postal stakeholders in an open, transparent and continuous process to improve cost accounting and cost attribution . . . , especially as it applies to competitive products.”)

The report of the Senate Committee on Governmental Affairs states:

[T]he Postal Service today is able to attribute less than 60 percent of its costs among its various products. This means that more than 40 percent of costs are labeled as institutional. The Postal Service itself admits that a disproportionate amount of these so-called institutional costs are paid for with revenue generated by First-Class Mail, which is covered by the postal monopoly The Committee agrees . . . that this situation should be improved. The Postal Service should be able to attribute a greater percentage of its costs. If they do this, it is likely that a greater share of costs can be attributed to competitive products and, to the extent that they can be, should be reflected in the rates charged for those products.

Id. at 29-30.

⁴⁹ The report of the Senate Committee on Governmental Affairs states:

The fact that the Committee believes the Postal Service can improve on its 60 percent attribution rate does not mean we believe the Postal Service should strive to attribute 100 percent of its costs, or any other arbitrary percentage. We also do not believe that the Postal Service should be forced to attribute such a large percentage of its costs to competitive products that those products will no longer be affordable and will no longer be made available to the customers who need them

Id. at 30.

The report of the House of Representatives' Committee on Government Reform states:

In addressing the attributable costs, the Commission should continue to focus on the need to have reliable indicators of cost causality. This Committee has heard testimony . . . urging a higher attribution of costs. The goal of the Commission should be a technically correct result, placing accuracy above achieving a particular outcome of higher or lower attribution.

H.R. Rep. No. 109-66, pt. 1, at 49.

risks associated with the over-attribution of costs apply equally to excessive price markups. Order No. 6043 at 68.

The PAEA's legislative history shows that the appropriate share requirement's language went from more to less prescriptive as postal reform legislation evolved. *Id.* House versions of the bill would have required Competitive products to make a "reasonable contribution" to institutional costs,⁵⁰ while Senate versions would have required Competitive products to cover "their share" of institutional costs.⁵¹ The "appropriate share" language that was ultimately enacted formed part of the compromise between the competing versions of postal reform that produced the PAEA.⁵² This language shows that the focus of the appropriate share requirement was not simply on ensuring a particular level of institutional cost coverage, which is what the Senate version of postal reform would have accomplished by requiring Competitive products to recover "their share" of institutional costs. And, importantly, the PAEA's

⁵⁰ See, e.g., H.R. 4341, 108th Cong. (2004), H.R. Rep. No. 108-672, 108th Cong., pt. 1, at 86 (Sept. 8, 2004) (proposing to codify 39 U.S.C. § 3633(a)(3) "to ensure that all competitive products collectively make a reasonable contribution to the institutional costs of the Postal Service."); H.R. 22, 151 Cong. Rec. H6524 (daily ed. Jul. 26, 2005) (proposing the same text to the 109th Congress).

The House of Representatives' Committee on Government Reform reported on H.R. 4341 (the prior version of the bill introduced to the 108th Congress) and H.R. 22 (the version of the bill introduced to the 109th Congress), stating in both reports that "[w]ith respect to the requirement that competitive products collectively make a reasonable contribution to overhead, it should be noted that the broad standard contains inherent flexibility. It is not intended to dictate a particular approach that the Postal Regulatory Commission should follow." H.R. Rep. No. 108-672, pt. 1, at 8; H.R. Rep. No. 109-66, pt. 1, at 49.

⁵¹ See, e.g., S. 2468, 150 Cong. Rec. S5990, 108th Cong. (daily ed. May 20, 2004) (proposing to codify 39 U.S.C. § 3633(a)(3) to "ensure that all competitive products collectively cover their share of the institutional costs of the Postal Service"); S. 662, 152 Cong. Rec. S914 (daily ed. Feb. 9, 2006) (proposing the same text to the 109th Congress to be codified as 39 U.S.C. § 3633(a)(3)).

⁵² Similarly, the Senate version of postal reform proposed as a new objective for the Market Dominant ratemaking system that it "allocate the total institutional costs of the Postal Service equitably between market-dominant and competitive products."). S. 2468, 150 Cong. Rec. S5988, 108th Cong. (daily ed. May 20, 2004). In the final version of the PAEA that was enacted, however, "equitably" was changed to "appropriately," which is how Objective 9 currently appears at 39 U.S.C. § 3622(b)(9).

legislative history shows an intent to give the Postal Service pricing flexibility with respect to its Competitive products.⁵³

As the Commission has explained, after attributing costs at the product- and group-levels, it is not possible to further quantify the degree to which the remaining (institutional) costs are related to the provision of either Competitive products or Market Dominant products. Order No. 6043 at 73, 81-85. Institutional costs consist of a mixture of fixed costs and variable costs (referred to as unattributed inframarginal costs) that result from economies of scale and scope in the joint production of both Market Dominant and Competitive products. *Id.* at 81, 83-85. The existence of such costs is inevitable in a multiproduct firm with economies of scale and scope; it does not stem from insufficient data or costing techniques. *Id.* at 84, 85. Institutional costs are jointly caused by all of the Postal Service's products because they are network costs caused by the existence of a system in which Market Dominant and Competitive products are handled simultaneously.⁵⁴ However, they cannot be separately identified and linked to any specific product or group of products because the relationships between institutional costs and specific products or groups of products are not discernible or quantifiable. Order No. 6043 at 81, 82, 83, 84. As a result, there is no meaningful

⁵³ See S. Rep. No. 108-318, at 1 ("[The PAEA] gives the Postal Service the authority to set rates for competitive products . . . as long as these prices do not result in cross-subsidy from the market-dominant products."); *id.* at 7 ("[T]he Postal Service's Board of Governors is permitted to more directly manage and price the Postal Service's competitive products; subject to minimal Regulatory Commission oversight to ensure that the Postal Service competes fairly with the private sector delivery services."); *id.* at 41 ("With respect to competitive products, the Postal Service is given pricing flexibility comparable to that exercised by private competitors."); H.R. Rep. No. 109-66, pt. 1, at 44 ("The Postal Service will be given flexibility to price competitive products, but without subsidy from market-dominant mail revenues.").

⁵⁴ *Id.* at 82, 83, 84. See John C. Panzar, *Protecting the Package Delivery Market and the Economy from Distortions Resulting from Fully-Distributed Cost Pricing*, October 2020, at 22, available at <https://www.packagecoalition.org/resources/other/file/PP-2020-10-Panzar-Protecting-the-Package-Delivery-Market-from-FDC-Pricing-distortions.pdf> (2020 Panzar Paper).

relationship between any of the costs currently classified as institutional and any products or groups of products, including Competitive products.⁵⁵

Due to the lack of any meaningful relationship between institutional costs and any specific products or group of products, trying to allocate institutional costs to products would be inherently arbitrary. Order No. 6043 at 83. Such an effort would be functionally identical to fully distributed costing, which is a methodology that has been widely discredited by expert economists as economically unsound for use with respect to the Postal Service and would run counter to Congress's express intent of ensuring accuracy in postal costing. *Id.* at 85-91. As previously explained, undertaking this exercise would directly contradict the text of 39 U.S.C. § 3631(b).⁵⁶ Moreover, adopting UPS's position that the only way to protect fair competition in the market for competitive postal services is for a significant portion of institutional costs to be allocated to Competitive products in a manner identical to fully distributed costing (see UPS Comments at 43-44) would effectively limit the Postal Service's pricing flexibility in contravention of the intent of the PAEA's overall policy with respect to Competitive products. Order No. 6043 at 47, 65. Moreover, the "problems" that UPS's interpretation purports to solve do not actually exist because the relevant market is healthy. See Section V.B.2., *infra*.

⁵⁵ Order No. 6043 at 81, 82, 83, 84. This specifically responds to the court's question "[a]re some of the Postal Service's institutional costs – and especially its unattributed inframarginal costs – still *related in some meaningful way to competitive products*, even if those costs cannot be attributed under [39 U.S.C.] § 3633(a)(2)?" *UPS II*, 955 F.3d at 1045 (emphasis added).

⁵⁶ Order No. 6043 at 85 n.131. The legislative history also rejects such an exercise. See S. Rep. No. 108-318, at 9-10, 29; H.R. Rep. No. 109-66, pt. 1, at 49. Although UPS attempts to argue that its approach does not constitute fully distributed costing because it does not assign all costs to individual products and merely seeks to "ensure fair competition and fiscal responsibility[]" as "mandated by the [PAEA][,]" (UPS Comments at 43-44), UPS fails to rebut the Commission's detailed explanation for how the UPS approach is "functionally identical to the economic concept of fully distributed costing[,]" and that "the impact of such an exercise on Competitive products and the Postal Service is the same as if it were applied to the entire firm." Order No. 6043 at 86.

The foregoing considerations all lead the Commission to conclude that UPS's interpretation of the appropriate share requirement's purpose is not what Congress intended. The Commission's interpretation articulated in Order No. 6043, however, accounts for the full text and structure of 39 U.S.C. § 3633, as well as for the PAEA's purposes and legislative history. Properly contextualizing the appropriate share requirement clarifies all the alleged anomalies raised by UPS.

Ultimately, the debate is not whether the Postal Service's institutional costs should be recovered, but how the PAEA intended for them to be recovered. UPS treats the appropriate share requirement as if it were a ceiling instead of a floor, which is inconsistent with the text, structure, purpose, and legislative history of the PAEA. See, e.g., UPS Comments at 8, 31, 32; UPS Reply Comments at 14. At the same time, however, the Commission retains an appropriate share requirement in this periodic review to serve as a margin of safety against any possibility that the Postal Service's Competitive products could be anticompetitively priced, despite covering their attributable costs.⁵⁷

⁵⁷ Order No. 6043 at 62. Moreover, the dynamic formula-based approach to setting the appropriate share that the Commission is readopting implicitly considers the prevailing competitive conditions in the market, which are discussed at Section V.B.2., *infra*, and based on that consideration the final rule will raise the appropriate share requirement from the historical 5.5 percent level to 10.4 percent in FY 2023. FY 2021 ACD at 100.

For the foregoing reasons, considering the text, structure, and purpose of 39 U.S.C. § 3633, UPS has not demonstrated that the Commission's interpretation would be unambiguously foreclosed.⁵⁸ Nor has UPS established that any ambiguity exists in 39 U.S.C. § 3633(a)(3) or (b) as to whether the appropriate share requirement was intended to serve as a less economically-rigorous form of cost allocation than that already performed pursuant to 39 U.S.C. § 3633(a)(1) and (2). Finally, even if such ambiguity were found to exist (which it does not), the statutory text, structure, purpose, and legislative history illustrate that the Commission's interpretation is reasonable and permissible.⁵⁹

C. Preventing Subsidization is Not the Appropriate Share Provision's Primary Purpose

1. Comments

UPS contends that the purpose of the appropriate share requirement is "to ensure fair competition with a level playing field and to prevent subsidization[]" by requiring the Postal Service's Competitive product business to recover "all of the institutional costs associated with that business[,] apportion[ing] costs in a . . . manner that ensures total cost coverage" UPS Comments at 9, 16, 36. UPS asserts that

⁵⁸ Order No. 6043 at 92-95; See, e.g., *Petit*, 675 F.3d at 781 (to prevail under *Chevron* step one, a challenger "must do more than offer a reasonable or, even the best, interpretation [of the statute in question]." (quoting *Village of Barrington, Ill. v. Surface Transp. Bd.*, 636 F.3d 650, 661 (D.C. Cir. 2011)) (internal marks omitted). "Instead, they 'must show that the statute *unambiguously* forecloses the [agency's] interpretation.'" *Petit*, 675 F.3d at 781 (emphasis in original) (quoting *Village of Barrington*, 636 F.3d at 661). "[T]hey must demonstrate that the challenged term is susceptible of only [one] possible interpretation." *Petit*, 675 F.3d at 781 (quoting *Shalala*, 192 F.3d at 1015 (internal marks and citation omitted)).

⁵⁹ At *Chevron* step two, courts "ask 'whether the agency's [interpretation] is based on a permissible construction of the statute.'" *Petit*, 675 F.3d at 785 (quoting *Chevron*, 467 U.S. at 843). Courts consider "whether the [agency] has reasonably explained how the permissible interpretation it chose is 'rationally related to the goals of' the statute." *Id.* (quoting *Village of Barrington*, 636 F.3d at 665 (internal marks omitted)). "If the statute is ambiguous enough to permit the agency's reading, . . . [courts will generally] defer to that interpretation so long as it is reasonable." *Nat'l Cable & Telecomms. Ass'n v. FCC*, 567 F.3d 659, 663 (D.C. Cir. 2009) (citing *Consumer Elecs. Ass'n*, 347 F.3d 299).

“private firms must recover *all* of the types of costs that the Postal Service classifies as institutional to stay in business[.]” (emphasis in original), and “[t]he playing field is not level when the Postal Service is not required to do the same.” UPS Reply Comments at 14. The result, according to UPS, is “market-dominant products . . . effectively subsidizing competitive products.” UPS Comments at 40. UPS argues that “subsidization” is not limited to the failure to recover attributable costs, but can also occur “where market-dominant products cover more than their fair share of institutional costs” *Id.*

UPS argues that incremental costs, which currently form the price floors under 39 U.S.C. § 3633(a)(1) and (a)(2), are not necessarily sufficient to prevent subsidization. UPS Reply Comments at 26. UPS argues that 39 U.S.C. § 3633(a)(1) and (a)(2) are insufficient safeguards because the Postal Service only considers incremental costs in the short run, and the Postal Service, by virtue of having operated at a loss for some years now, cannot be said to have passed the incremental cost test at an enterprise-wide level, meaning that it cannot definitively be said that the Postal Service’s rate structure is subsidy-free. *Id.* at 26-27. UPS contends that Congress’s intent in enacting 39 U.S.C. § 3633(a)(3) and (b) was to prevent this type of subsidization.⁶⁰

The Postal Service, ASL, Dr. Panzar, and Pitney Bowes all argue that the price floors established under 39 U.S.C. § 3633(a)(1) and (a)(2), which are based on incremental costs, are sufficient to prevent subsidization and unfair competition.⁶¹ ASL asserts that UPS “incorrectly challenges the sufficiency of the incremental cost

⁶⁰ UPS Comments at 35 (“The [PAEA’s] concern with fair competition . . . is . . . about a government agency expanding to compete into the private sector”); *id.* at 36 (“Congress directed the Commission to ensure that the Postal Service’s package delivery business must stand on its own, and cover all of its associated costs.”); UPS Reply Comments at 15 (“[W]hile Congress wanted to give the Postal Service increased flexibility, that flexibility came at a price—the Commission must ensure that the Postal Service does not engage in strategies that allow it to exploit its status as a government-sponsored monopolist in certain products to distort private-sector competition in other products.”).

⁶¹ Postal Service Reply Comments at 41, 48-49; ASL Comments at 20; ASL Reply Comments at 13; Panzar Decl. at 14; Pitney Bowes Comments at 9; Pitney Bowes Reply Comments at 6.

test . . . while conflating the prohibition against cross-subsidization with the price floor under section 3633(a)(3).” ASL Reply Comments at 13. ASL and the Public Representative argue that UPS’s interpretation of the appropriate share requirement’s purpose would, by mandating total recovery of institutional costs, have the effect of reimposing a break-even requirement. *Id.* at 9; PR Reply Comments at 6. ASL, Pitney Bowes, and the Public Representative assert that UPS treats the appropriate share as if it were a ceiling, as opposed to a floor.⁶²

The Lexington Institute (LI) reads the Commission’s interpretation of the purpose of the appropriate share provision from Order No. 6043 as being “solely concerned with protecting the Postal Service’s competitive position, even if that will lead to financial losses” LI Comments at 2.

2. Commission Analysis

UPS’s claim that the primary purpose of the appropriate share is to prevent Market Dominant products from subsidizing Competitive products (see UPS Comments at 40) is contravened by the plain language and structure of the statute. The text of 39 U.S.C. § 3663(a)(3) and the considerations for the Commission to review under 39 U.S.C. § 3633(b) lack any reference to such a concern. Instead, the PAEA establishes the permanent requirements that the Commission promulgate regulations to “prohibit the subsidization of competitive products by market-dominant products” pursuant to 39 U.S.C. § 3633(a)(1) and “ensure that each competitive product covers its costs attributable” pursuant to 39 U.S.C. § 3633(a)(2), as well as the provisions governing the

⁶² ASL Reply Comments at 8; Pitney Bowes Reply Comments at 9; PR Reply Comments at 7-8.

regulation of Market Dominant products pursuant to 39 U.S.C. § 3622.⁶³ It is implausible that Congress—having required the Commission to prohibit the subsidization of Competitive products by Market Dominant products under 39 U.S.C. § 3633(a)(1)—also intended to mandate an additional level of protection against subsidization via the appropriate share provision, while at the same time explicitly authorizing the Commission to eliminate the appropriate share entirely.

Furthermore, all the same textual, structural, contextual, and historical bases that the Commission identified in rejecting UPS's argument that the purpose of the appropriate share requirement is primarily directed at institutional cost allocation apply equally to UPS's argument that the purpose of the appropriate share requirement is primarily directed at preventing subsidization. See Section IV.B.2., *supra*. Nevertheless, although the Commission does not accept that the purpose of 39 U.S.C. § 3633(a)(3) and (b) is to prohibit subsidization, the Commission has considered UPS's argument that the appropriate share should be set at a level consistent with fully

⁶³ The PAEA charges the Commission with the establishment and periodic revision of the contours of a modern ratemaking system for Market Dominant products. See 39 U.S.C. § 3622(a). The PAEA enumerates 9 specific “objectives” that the Market Dominant ratemaking system shall be designed to achieve, and 14 specific “factors” that the Commission must take into account in establishing or revising the Market Dominant ratemaking system. See *generally* 39 U.S.C. § 3622(b) and (c). The Postal Service's ability to set rates for its Market Dominant products is subject to limitations that do not apply to its Competitive products, such as a cap on price increases and limitations related to workshare discounts. See 39 U.S.C. § 3622(d)(1)(A) and (e). Based on a finding that the ratemaking system has not achieved the statutory objectives, taking into account the statutory factors, the Commission recently modified the ratemaking system “as necessary to achieve the objectives,” which, in part, provided for discrete amounts of additional rate authority. Docket No. RM2017-3, Order Adopting Final Rules for the System of Regulating Rates and Classes for Market Dominant Products, November 30, 2020, at 37 (quoting 39 U.S.C. § 3622(d)(3)) (Order No. 5763). The objectives and factors encompass multiple priorities including pricing flexibility, increased efficiency, stable rates, and providing classifications with extremely high degrees of reliability and speed of delivery, among other things. Additionally, the Commission was required to establish Market Dominant ratemaking system regulations that took into account “the requirement that each class of mail or type of mail service bear the direct and indirect postal costs attributable to each class or type of mail service through reliably identified causal relationships plus that portion of all others costs of the Postal Service reasonably assignable to such class or type.” 39 U.S.C. § 3622(c)(2). The Market Dominant ratemaking system was also required to be designed so that the total institutional costs of the Postal Service would be allocated appropriately between Market Dominant and Competitive products. 39 U.S.C. § 3622(b)(9).

distributed costing (which in UPS's view is the only adequate protection against subsidization). In the Commission's judgment, the existing incremental cost-based methodology for testing for subsidization of Competitive products by Market Dominant products is more than sufficient to prevent subsidization and completely resolves this concern. Order No. 6043 at 26; see Section V.A.3.b., *infra*.

The consideration of long-term incremental costs and/or "the long-term, structural changes the Postal Service would make if it did not deliver packages[]" are not relevant to the question of subsidization. UPS Reply Comments at 27. UPS argues that in the absence of Competitive products, "[w]ith ever decreasing letter volumes, if the Postal Service were profit-maximizing, it would take the hard steps required to right-size the business and *decrease* the scope and frequency of its delivery network." *Id.* (emphasis in original). Thus, to UPS, "the analytically correct method for evaluating incremental costs would consider the degree to which the Postal Service's institutional costs would be reduced through an efficient reorganization of the enterprise if the Postal Service did not deliver packages" *Id.* at 30. The premise underlying this argument is that the Postal Service's network could be substantially restructured if the Postal Service did not offer Competitive products, and therefore the difference in cost between the current network and what UPS hypothesizes the network might look like in the absence of Competitive products can be thought of as being associated with Competitive products. This underlying premise (and by consequence, all UPS's arguments reliant on this premise) is flawed because it ignores the legal restrictions on the Postal Service's ability to decrease the scope and frequency of its network that are outside the Postal Service's control. The requirements of the Postal Service's network, including the network's scope and frequency, are largely driven by legal obligations. As part of its universal service obligation, the Postal Service is legally required to deliver mail "at least six days a week[.]" 39 U.S.C. § 101(b), and the Postal Service is legally required to provide

postal services to all parts of the United States, regardless of location, size, or density.⁶⁴ These legal requirements would remain even if the Postal Service did not deliver any Competitive products. Unlike a private firm, the Postal Service is severely limited in its ability to implement many of the types of hypothetical efficiencies that the long-term incremental costing called for by UPS would be premised upon, such as reducing the scope or frequency of the Postal Service's network. This does not in any way indicate "subsidization" of Competitive products by Market Dominant products. See Section VIII.C.3., *infra*. Nor is the allegation that the Postal Service could not pass the incremental cost test at an enterprise-wide level relevant to compliance with 39 U.S.C. § 3633(a)(1) and (a)(2), which require only that Competitive products cover their incremental costs (collectively and individually, respectively). Market Dominant products operate under a different (and much more restrictive) regulatory regime with respect to pricing, and the Postal Service's financial problems with respect to its Market Dominant products are well known.⁶⁵

Moreover, UPS mischaracterizes the manner in which institutional costs are recovered by suggesting that the Postal Service increases Market Dominant product prices to ameliorate the failure of Competitive products prices to generate sufficient

⁶⁴ See, e.g., 39 U.S.C. § 101(a) ("The . . . Postal Service . . . shall provide prompt, reliable, and efficient services to patrons *in all areas* and shall render postal services *to all communities*." (emphasis added)); 39 U.S.C. § 101(b) ("The Postal Service shall provide a maximum degree of effective and regular postal services *to rural areas, communities, and small towns where post offices are not self-sustaining*." (emphasis added)); 39 U.S.C. § 101(b) ("[I]t [is] the specific intent of the Congress that effective postal services be insured to residents *of both urban and rural communities*." (emphasis added)); 39 U.S.C. § 403(a) ("The Postal Service shall receive, transmit, and deliver *throughout the United States, its territories and possessions . . .*" (emphasis added)); 39 U.S.C. § 403(a) ("The Postal Service shall serve as nearly as practicable *the entire population of the United States*." (emphasis added)). See also Postal Regulatory Commission, *Report on Universal Postal Service and the Postal Monopoly*, December 19, 2008, at 18-33 (USO Report).

⁶⁵ See Order No. 6043 at 34-35, 64. See also generally Order No. 5763; Docket No. RM2017-3, Order on the Findings and Determination of the 39 U.S.C. § 3622 Review, December 1, 2017 (Order No. 4257).

revenue to cover their fair share of institutional costs.⁶⁶ In actuality, because the Market Dominant price cap constrains the amount of contribution to institutional costs that can be obtained from Market Dominant product revenues, the Postal Service *must* look to Competitive products for the difference. Order No. 6043 at 61. LI similarly mischaracterizes the Commission's interpretation as "solely concerned with protecting the Postal Service's competitive position." LI Comments at 2. As explained above, the Commission's interpretation supports the PAEA's multi-faceted purpose for Competitive product regulation, which focuses on Competitive product cost coverage to safeguard fair competition in the market for competitive postal services, while at the same time not unduly restraining competitive conduct in the market by the Postal Service.⁶⁷

In sum, considering 39 U.S.C. § 3633's text, structure, and purpose, commenters have failed to demonstrate that the Commission's interpretation would be unambiguously foreclosed or that any statutory ambiguity exists regarding the prohibition of subsidization. Finally, even if such ambiguity were found to exist (which it does not), the statutory text, structure, purpose, and legislative history illustrate that the Commission's interpretation is reasonable and permissible.

⁶⁶ See UPS Comments at 40; UPS Brief at 50-51. The Commission disputes the premise that the Postal Service underprices its Competitive products or has engaged anticompetitive behavior. See Order No. 6043 at 92-94, 104. Moreover, the Commission has explained the very real risk of harm posed by the prospect of setting a price floor pursuant to 39 U.S.C. § 3633(a)(3) (which is designed to function as a minimum contribution level) too high to over-correct for a highly theoretical harm. See *id.* at 61. The Commission explained how its dynamic formula-based approach accounts for any potential anticompetitive behavior or underpricing, as well as avoiding setting the appropriate share too high. See *id.* at 94, 104-05.

⁶⁷ See Section IV.B.2.b., *supra*. See also Order No. 6043 at 57, 62-63. If a competitive deficit existed (which it does not), the Commission would take that circumstance into account as part of its determination as to what the appropriate share should be. See Order No. 6043 at 105-09.

D. The Objective Appearing in 39 U.S. Code Section 3622(b) is Not Relevant to the Appropriate Share Review

1. Comments

In addition to 39 U.S.C. § 3633, UPS cites 39 U.S.C. § 3622(b)(9) as further statutory authority for its positions regarding the appropriate share provision's purpose. UPS Comments at 1, 32, 42; UPS Reply Comments at 3. This provision states that the ratemaking system for Market Dominant products shall be designed to achieve nine specific objectives in conjunction with each other, one of which is "[t]o allocate the total institutional costs of the Postal Service appropriately between market-dominant and competitive products." 39 U.S.C. § 3622(b)(9). The Postal Service, the Public Representative, and Pitney Bowes argue that 39 U.S.C. § 3622(b)(9) has no relevance to the appropriate share.⁶⁸

2. Commission Analysis

With respect to UPS's contention that its argument is supported by 39 U.S.C. § 3622(b)(9), the Commission concludes that that provision has no relevance to the Commission's appropriate share determination under 39 U.S.C. § 3633(a)(3) and (b). Section 39 U.S.C. § 3622(b)(9) constitutes one of nine objectives to be balanced in conjunction with each other whenever the Commission establishes, revises, modifies, or adopts an alternative ratemaking system for Market Dominant products. *See generally* 39 U.S.C. § 3622. This provision does not apply or require any regulatory action with respect to the Competitive product ratemaking system. *Compare* 39 U.S.C. § 3622, *with* 39 U.S.C. § 3633. UPS has failed to demonstrate that this provision compels UPS's alternative interpretation of the appropriate share requirement's purpose or that it would unambiguously foreclose the Commission's interpretation of the same or that

⁶⁸ Postal Service Reply Comments at 62-63; PR Reply Comments at 9; Pitney Bowes Reply Comments at 6.

there is any ambiguity as to the potential relevance of the Market Dominant ratemaking system objectives contained at 39 U.S.C. § 3622(b) with respect to the statutory scheme for Competitive products. Moreover, UPS's interpretation of 39 U.S.C. § 3622(b)(9) is fundamentally flawed because if allocating all the Postal Service's institutional costs was indeed a requirement, then it would produce a statutory conflict with 39 U.S.C. § 3633(b), which unambiguously authorizes the Commission to eliminate the appropriate share. *Compare* 39 U.S.C. § 3622(b)(9), *with* 39 U.S.C. § 3633(b). See Pitney Bowes Reply Comments at 6.

E. Prior Commission Statements Do Not Foreclose Use of the Dynamic Formula-Based Approach

1. Comments

UPS asserts that the Commission's interpretation of the appropriate share requirement's purpose as articulated in Order No. 6043 is inconsistent with statements the Commission has made in Order No. 1449. See UPS Comments at 34-35; UPS Reply Comments at 13-14.

2. Commission Analysis

In Order No. 1449, the Commission stated that “[a] primary function of the appropriate share requirement is to ensure a level playing field in the competitive marketplace.” Order No. 1449 at 13. The Commission explained that “[t]he appropriate share requirement could be said to represent the fixed costs of the competitive enterprise and should reflect the ways in which institutional resources are spent on the competitive enterprise[,]” and “[i]f the Postal Service's competitive products were not required to contribute an appropriate share towards the institutional costs of the enterprise, this could result in the market dominant products cross-subsidizing the fixed costs of the stand-alone competitive enterprise.” *Id.*

The statements identified by UPS do not prevent the Commission from issuing a final rule based on the dynamic formula-based approach in this docket. It is important to recognize that these statements were made before the adoption of the incremental cost test in Final Order No. 3506 which allowed the Commission to significantly expand cost attribution and reduce institutional costs. See Order No. 6043 at 27-35. Final Order No. 3506 led to certain costs that were classified as institutional (at the time of the PAEA's enactment and the issuance of Order No. 1449) being reclassified as attributable after the issuance of Final Order No. 3506.⁶⁹ This reclassification increased the price floors applied to individual Competitive products pursuant to 39 U.S.C. § 3633(a)(2), which prevents cross-subsidization of individual Competitive products by other Competitive products, and the price floor applied to Competitive products collectively pursuant to 39 U.S.C. § 3633(a)(1), which prohibits the subsidization of Competitive products by Market Dominant products. See *id.* If the Commission had not made the decision to reclassify these costs as attributable, then under the interpretation of "uniquely or disproportionately associated" costs that the Commission articulated in Order No. 6043, these costs would have been relevant to the Commission's appropriate share determination. *Id.* at 79-80. Thus, the statements appearing in Order No. 1449 were made before the Commission was able to adopt the incremental cost test to test for cross-subsidizes in Final Order No. 3506; and thus do not fully reflect the Commission's current conception of institutional costs.⁷⁰

It is also relevant that the statements appearing in Order No. 1449 were made upon conclusion of the first periodic review of the appropriate share. See *generally* Order No. 1449. The Commission acknowledges that these statements, made

⁶⁹ Specifically, expanding cost attribution reduced institutional costs because product-level inframarginal cost, group-specific cost, and group-level inframarginal costs were no longer classified as institutional. See Order No. 6043 at 30.

⁷⁰ See Order No. 6043 at 25-27 (describing initial efforts to calculate incremental costs by the Commission and its predecessor agency (the former Postal Rate Commission)).

immediately following the first 5 years of the PAEA era during which the appropriate share was mandatory, did not discuss the Commission's express authority to eliminate the appropriate share requirement pursuant to 39 U.S.C. § 3633(b).⁷¹ For this reason, in retrospect it would have been more accurate for Order No. 1449 to have referred to "contribution from Competitive products," rather than the "appropriate share requirement." If the Postal Service's Competitive products did not contribute to the Postal Service's institutional costs, then that could result in a competitive imbalance in the market for competitive postal services. The appropriate share requirement is a mechanism that enables the Commission to prevent and/or correct such a market imbalance by increasing the collective price floor for Competitive products.

Further, Order No. 1449 never suggested that it was necessary to arbitrarily allocate institutional costs into the price floor for Competitive products (which is what UPS proposes) to prevent cross-subsidization. Again, the need to protect competition must be balanced against Congress's intent to provide the Postal Service with pricing flexibility, particularly where the Postal Service is already pricing its Competitive products such that their contribution to institutional costs exceeds the required minimum and no evidence indicates a competitive imbalance exists in the market for competitive postal services.⁷²

As discussed above, the Commission's prior statements made in Order No. 1449 neither compel adoption of the position taken by UPS nor conflict with the more fulsome articulation of the appropriate share requirement's purpose appearing in Order No.

⁷¹ It is also worth noting that in the first review of the appropriate share (which culminated in Order No. 1449) no party argued for the existence of any uniquely or disproportionately associated costs, and the Commission "[did] not independently find any" Order No. 1449 at 14 n.14. As a result, the Commission in that docket was not required to fully address the issue in the way that it has been required to do in the instant docket.

⁷² See Order No. 6043 at 93, 105-09. Order No. 6043 traced actual contribution through FY 2020, when it covered 31.1 percent of all institutional costs. *Id.* at 93. In FY 2021, the most recent fiscal year for which data are available, Competitive product contribution covered 39.2 percent of total institutional costs. FY 2021 ACD at 96.

6043. Nonetheless, “[a]gencies are free to change their existing policies as long as they provide a reasoned explanation for the change.”⁷³ The agency must explain “that the new policy is permissible under the statute, that there are good reasons for it, and that the agency believes it to be better.”⁷⁴ To the extent that the Commission’s interpretation articulated in Order No. 6043 is viewed as a change in policy from Order No. 1449, the PAEA authorizes the Commission to rely on 39 U.S.C. § 3633(a)(1) and (2) as the primary safeguards against subsidization of Competitive products (collectively and individually, respectively). Doing so is consistent with the text, structure, and purpose of the PAEA, as well as a logical clarifying development to postal costing after the adoption of the incremental costs test in Final Order No. 3506. No reliance interests are implicated by these prior statements because, as described above, the prior statements did not expressly speak to the instant issue and because the statute expressly requires the Commission to consider the very prospect of eliminating, modifying, or retaining the appropriate share every 5 years.⁷⁵

F. The Commission Properly Considered the Degree to Which Any Costs are Uniquely or Disproportionately Associated with Any Competitive Products

1. Comments

UPS takes issue with the Commission’s interpretation of the “uniquely or disproportionately associated” phrase from 39 U.S.C. § 3633(b). UPS argues that the Commission conflates the “uniquely or disproportionately associated” phrase with the “reliably identified causal relationships” standard for cost attribution under 39 U.S.C.

⁷³ *Encino Motorcars, LLC v. Navarro*, 579 U.S. 211, 221 (2016) (citing *Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs.*, 545 U.S. 967, 981-82 (2005)).

⁷⁴ *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009) (emphasis omitted); see *Nat’l Ass’n of Home Builders v. EPA*, 682 F.3d 1032, 1038 (D.C. Cir. 2012).

⁷⁵ See *Encino Motorcars*, 579 U.S. at 221-22 (citing *Fox Television Stations, Inc.*, 556 U.S. at 515).

§ 3631(b). UPS Comments at 13-14. UPS argues that the Commission's use of "economically sound" measurement fails to give the more expansive application to the "uniquely or disproportionately associated" phrase that UPS believes was mandated by the D.C. Circuit's remand opinion and conflicts with UPS's view of the appropriate share requirement's purpose.⁷⁶ UPS asserts that "[t]he Commission has approved numerous Postal Service costing methodologies that rely on imperfect estimations, judgments, and assumptions[.]" and that "[n]one of these . . . would meet the extreme degree of economic 'soundness' that the Commission now says it must require in setting the appropriate share." UPS Comments at 14-15.

ASL, Dr. Panzar, and Pitney Bowes all find the Commission's interpretation of the "uniquely or disproportionately associated" phrase to be reasonable.⁷⁷ The Postal Service concurs that the "economically sound" measurement "is the only rational way to address the issue as framed by the terms of the remand opinion." Postal Service Comments at 19-20. The Postal Service, ASL, and Dr. Panzar argue that the Commission's interpretation does not run counter to the D.C. Circuit's instructions on remand because the D.C. Circuit did not mandate any particular outcome; it simply directed the Commission to explain how the "reliably identified causal relationships" standard and the "uniquely or disproportionately associated" phrase could coincide in application.⁷⁸ Dr. Panzar in particular notes that unlike the "reliably identified causal relationships" standard, there is no established economic or legal definition for "association," as opposed to "causation." Panzar Reply Decl. at 4.

The Postal Service asserts that the appropriate share is a pricing exercise, not a costing approach, and "[b]y its very nature, pricing is inherently more subjective and

⁷⁶ UPS Comments at 13-16. Arguments focusing on the purpose of the appropriate share are discussed above. See Sections IV.B.2., IV.C.2., *supra*.

⁷⁷ ASL Comments at 29; Panzar Decl. at 26-27; Pitney Bowes Comments at 11.

⁷⁸ Postal Service Reply Comments at 33-35; ASL Reply Comments at 2-3; Panzar Reply Decl. at 3-5.

judgmental than costing, which the statute requires [to] be conducted subject to the ‘reliable causation’ standard.” Postal Service Reply Comments at 47-48.

2. Commission Analysis

The Commission rejects UPS’s contention that the Commission’s interpretation of the “uniquely or disproportionately associated” phrase articulated in Order No. 6043 conflates that statutory phrase with the “reliably identified causal relationships” standard for cost attribution from 39 U.S.C. § 3631(b). The Commission must “consider all *relevant* circumstances, including . . . the *degree to which* any costs are uniquely or disproportionately associated with any competitive products.” 39 U.S.C. § 3633(b) (emphasis added). This language explicitly confers discretion on the Commission to fill in any gaps with respect to relevance and/or the degree of relationship. See Order No. 6043 at 54-57.

Consistent with the court’s instruction in *UPS II*, the Commission exercised this discretion and clarified that the scope of costs encompassed by the phrase “uniquely or disproportionately associated” in 39 U.S.C. § 3633(b) is broader than, but largely overlaps in application with, the scope of costs encompassed by the phrase “reliably identified causal relationships” in 39 U.S.C. § 3631(b). *Id.* at 52-53 (citing *UPS II*, 955 F.3d at 1049-50).

Because the statutory phrases are overlapping, the Commission declined to account for costs meeting the definition of both phrases more than once in setting the collective Competitive product price floor under 39 U.S.C. § 3633(a)(3).⁷⁹ To be incorporated into the Commission’s appropriate share determination, a cost must be

⁷⁹ *Id.* at 55-56. The sum of the individual product price floors required by 39 U.S.C. § 3633(a)(2) is included within the calculation of the additional price floor required by 39 U.S.C. § 3633(a)(1) (which is applied to Competitive products as a whole). *Id.* at 5, 32, 75. The price floor set by the Commission pursuant to 39 U.S.C. § 3633(a)(3) is the sum of the collective price floor required by 39 U.S.C. § 3633(a)(1) plus the appropriate share. See *id.* at 8, 32.

capable of being measured in a manner that is economically sound. *Id.* at 54. The Commission found this approach to be “a reasonable policy and technical judgment in light of the harms that would be likely to result from attempting to account for or allocate a portion of institutional costs . . . in some arbitrary manner[].” *Id.*

The Commission’s basis for exercising this discretion was reasonably explained in Order No. 6043.⁸⁰ The different interrelated price floors under 39 U.S.C. § 3633(a) require Competitive product prices to be set high enough to generate revenue that would meet or exceed costs attributable to Competitive products at the individual product and group levels and an appropriate share of the Postal Service’s institutional costs. See Order No. 6043 at 7-8, 31 n.49, 32, 75-76. The requirement to “consider *all relevant* circumstances, including . . . *the degree to which* any costs are uniquely or disproportionately associated with any competitive products” (39 U.S.C. § 3633(b) (emphasis added)) does not require the Commission to rely on arbitrary allocations of costs (as suggested by UPS) (see Sections VIII.A.3., VIII.B.3., VIII.C.3., VIII.D.3., *infra*) rather than using economically sound measurement as developed by the Commission. Moreover, arbitrarily allocating some institutional costs to the Competitive product price floor would be inconsistent with the purpose of the appropriate share requirement by limiting the Postal Service’s pricing flexibility and potentially harming its ability to compete and maximize Competitive product contribution to institutional costs. See Section IV.B.2., *supra*.

Consistent with the D.C. Circuit’s remand opinion, the Commission has reviewed all the Postal Service’s accrued costs to determine the extent to which any of them can be said to be uniquely or disproportionately associated with any Competitive products. The Commission has not identified any existing costs other than those that also meet

⁸⁰ *Northwestern Corp. v. Fed. Energy Regul. Comm’n*, 884 F.3d 1179, 1181 (D.C. Cir. 2018) (under the Administrative Procedure Act’s arbitrary and capricious standard, an agency’s decision must be reasonable and reasonably explained).

the narrower “reliably identified causal relationships” standard for cost attribution and are thus already being attributed to Competitive products. See Section V.A.5., *infra*. The Commission has also reviewed each of the specific types of costs alleged by commenters to be “uniquely or disproportionately associated” with Competitive products, and has concluded that none of those costs are, in fact, uniquely or disproportionately associated with Competitive products. See Section VII., *infra*.

As the Commission has explained, the adoption of group-level incremental costs for purposes of cost attribution in Docket No. RM2016-2 essentially aligned the field of costs encompassed by “reliably identified causal relationships” standard under 39 U.S.C. § 3631(b) and (a)(2) with the field of costs encompassed by the test for cross-subsidy under 39 U.S.C. § 3633(a)(1) and with the broader field of costs that might once have been considered “uniquely or disproportionately associated” with Competitive products despite not formerly being attributed to them. Order No. 6043 at 31, 79-80. Group-level incremental costs represent the outer limits of costs that can be linked with specific products or groups of products in any way using existing costing methodologies.

However, while the Commission has conceded that the “uniquely or disproportionately associated” and “reliably identified causal relationships” phrases are at the present time largely overlapping in application, the Commission has nevertheless articulated a principled and reasonable distinction between them, which the Commission demonstrated in Order No. 6043 with the example of product-level inframarginal, group-specific, and group-level inframarginal costs. As the Commission explained, at the time of the PAEA’s enactment, not all the cost categories that the Commission now considers attributable were attributed. *Id.* at 79-80. Specifically, the way attributable costs were calculated at that time did not include inframarginal costs. *Id.* at 27-33. However, after the issuance of Final Order No. 3506, the Commission began using incremental costs as the basis for cost attribution, which expanded

attributable costs to include product-level inframarginal, group-specific, and group-level inframarginal costs calculated as part of Competitive products' incremental costs. *Id.* at 29-30. As the Commission explained in Order No. 6043, if the Commission had not made the decision to reclassify these costs as attributable, then under the interpretation of "uniquely or disproportionately associated" costs that the Commission articulated in Order No. 6043, these costs would be relevant to the Commission's appropriate share determination. *Id.* at 79-80. Costs incremental to the provision of Competitive products exhibit an economically sound relationship with Competitive products. After the implementation of the incremental costs test for cost attribution, there are no costs uniquely or disproportionately associated with Competitive products other than those that are also classified as attributable. Thus, at the present time the "uniquely or disproportionately associated" and "reliably identified causal relationships" phrases do effectively coincide in application.

The Commission's interpretation is consistent with *UPS II*. The court directed the Commission to: (1) "explain why [the 'uniquely or disproportionately associated' and 'reliably identified causal relationships'] phrases have the same practical reach, despite the use of different language[];" (2) "consider all costs uniquely or disproportionately associated with competitive products in setting the appropriate share, even if [the Commission] has already accounted for those costs under § 3633(a)(1) and (a)(2)[];" (3) explain whether "there may be institutional costs that are 'uniquely or disproportionately associated with competitive products,' even though they cannot be said to stand in 'reliably identified causal relationships' with them[];" and (4) "explain the relevance (if any) of costs [the Commission] may have considered in implementing § 3633(a)(1)." *UPS II*, 955 F.3d at 1048-52. However, the court was clear that it "[did] not mean to render any decision on what the appropriate share determination under § 3633(a)(3) should be[.]" and that "the Commission might decide against revising its bottom-line judgment, given the other factors the Commission must consider under

§ 3633(b) and the latitude that the text affords the Commission in making a final determination.” *Id.* at 1048, 1051.

The Commission’s interpretation of the “uniquely or disproportionately associated” phrase is reasonable. UPS asserts that “[t]he Commission has approved numerous Postal Service costing methodologies that rely on imperfect estimations, judgments, and assumptions[,]” and that “[n]one of these . . . would meet the extreme degree of economic ‘soundness’ that the Commission now says it must require in setting the appropriate share.” UPS Comments at 14-15. However, proceedings to change costing methodologies are subject to different legal requirements than the pending appropriate share review. The Commission may conduct proceedings “to improve the quality, accuracy, or completeness of Postal Service data required by the Commission” where it appears that “the attribution of costs or revenues to products has become significantly inaccurate or can be significantly improved,” or if “such revisions are, in the judgment of the Commission, otherwise necessitated by the public interest.”⁸¹ To approve a proposed change, the Commission must find that the proposed change improves the quality, accuracy, or completeness of the data (or the analysis of data) in the annual periodic reports the Postal Service files with the Commission. 39 C.F.R. § 3050.11(a).

In the instant docket, by contrast, the Commission, consistent with the court’s instruction on remand and the text of 39 U.S.C. § 3633(b), uses sound economic measurement to determine which costs should be incorporated into the Commission’s determination of the appropriate share. See Order No. 6043 at 54; see also *UPS II*, 955 F.3d at 1045. This is “a reasonable policy and technical judgment in light of the harms that would be likely to result from attempting to account for or allocate a portion of

⁸¹ 39 U.S.C. § 3652(e)(2)(A), (C). Additional grounds for data improvement occur when “the quality of service data has become significantly inaccurate or can be significantly improved,” which does not apply here. 39 U.S.C. § 3652(e)(2)(B).

institutional costs . . . in some arbitrary manner[].” Order No. 6043 at 54-55. Adopting any of UPS’s four proffered alternatives would require the Commission to rely on an arbitrary methodology (rather than one that relies upon economics and cost accounting principles) and would be likely to lead to the harms identified in Order No. 6043.⁸² The examples of cost attribution methodologies that UPS cites as “imperfect” all involve reasonable estimations, judgments, and/or assumptions grounded in facts, observations, and logic.⁸³ It is reasonable for the costs associated with necessary support functions to be considered just as volume-variable as the function being

⁸² See Order No. 6043 at 80-95 (discussing potential harms). See *also* Section VIII., *infra* (discussing UPS’s proffered alternatives). To promulgate a rule that would not be set aside by a reviewing court for being “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law” pursuant to 5 U.S.C. § 706(2)(A), the Commission must present an adequate basis and explanation for its findings and conclusion. See, e.g., *State Farm Mut. Auto. Ins. Co.*, 463 U.S. at 34 (remanding National Highway Traffic Safety Administration order rescinding the passive restraint requirements of federal motor vehicle safety standard because the agency failed to present an adequate basis and explanation).

⁸³ UPS cites as examples situations in which the current cost attribution methodology employs “piggybacking” to identify, calculate and distribute costs to products. UPS Comments at 14-15. Piggybacking exploits the relationship between two cost components such that the piggybacked component is assumed to have the same volume variability and distribution to products as the primary component to which it is attached. Order No. 6043 at 20-21. UPS cites Cost Segment 12 (“Motor Vehicle Service”) (see UPS Comments at 15 n.17), which covers “salaries, benefits, and related costs of vehicle maintenance personnel work; expenses for supplies and services used in maintaining vehicles; expenses for fuel and lubricants; expenses for contracted maintenance services; and expenses for rented vehicles.” Summary Description of USPS Development of Costs by Segments and Components, Fiscal Year 2021, July 1, 2022, ZIP folder “Summary Description FY2021,” available at <https://www.prc.gov/dockets/document/122196> (FY21 Summary Descriptions), file “CS12-21.docx” at 12-1. UPS also cites Cost Segment 11 (“Custodial and Maintenance Services”) (see UPS Comments at 15 n.18), which covers “salaries, benefits, and related costs of custodial, operating equipment maintenance, and plant and building equipment maintenance personnel, and costs for contracted cleaning services.” FY21 Summary Descriptions, file “CS11-21.docx,” at 11-1. UPS argues that the Commission allows the Postal Service to assume that all vehicle- or equipment-related costs in these cost segments are volume-variable to the same extent as the labor using the vehicle or equipment, but “[t]he Commission has never made the Postal Service prove these assumptions were perfectly accurate.” UPS Comments at 15. UPS states, “[r]ather, [the Commission] has allowed the Postal Service to employ them as a reasonable way to *estimate* those costs that should be attributed to products.” *Id.* (emphasis in original). UPS states that “[t]here is no reason the Commission could not make similar estimates in setting the appropriate share.” *Id.* UPS also asserts that “more than 60 components or cost pools” contain an untested judgment by the Postal Service that costs are not volume-variable. *Id.* at 15-16. Finally, UPS argues that the Commission’s formula for determining the appropriate share would not pass the “economically sound” test because it is arbitrary and capricious. *Id.* at 16.

supported (as is the case with the activities in Cost Segments 11 and 12, which UPS cites (see UPS Comments at 15 n.17-18)). What UPS seeks with respect to the appropriate share—the allocation of costs to products without any economically meaningful basis for doing so—is unreasonable and is inconsistent with the PAEA. Although the use of “economically sound” measurement might conflict with UPS’s preferred interpretation of the PAEA, it is fully consistent with the appropriate share requirement’s multi-faceted purpose and role within the PAEA’s broader scheme and with the court’s instructions.

G. The Commission Reasonably Followed the Court’s Instruction to Consider Both Institutional and Attributable Costs

1. Comments

ASL suggests that the Commission’s interpretation of the “uniquely or disproportionately associated” phrase was, if anything, unduly favorable to UPS. ASL Reply Comments at 16. ASL states that:

[T]he Commission’s conclusion that the “uniquely or disproportionately associated” standard is broader [than the “reliably identified causal relationships” standard] is in no way compelled by the statutory language The section 3633(b) standard does not require consideration of *all* costs that might be associated with Competitive products, only those that are “*uniquely or disproportionately associated*” with Competitive products. . . .

Id. (emphasis in original).

The Postal Service, while it concedes that the Commission’s interpretation of the “uniquely or disproportionately associated” phrase articulated in Order No. 6043 is reasonable, suggests an alternative interpretation that it believes better reflects Congress’s intent. Postal Service Comments at 30-31. The Postal Service traces the origins of the “uniquely or disproportionately associated” phrase to a 1999 postal reform

bill which contained an “equal markup” approach to allocating institutional costs.⁸⁴ Under this approach, Competitive product rates collectively would have needed to have been set high enough so that the resulting ratio of overall Competitive product revenues to Competitive product attributable costs would have been at least as high as the overall ratio (across all products—Competitive and Market Dominant) of revenue to attributable costs.⁸⁵ The logic underlying this requirement, according to the Postal Service, was that attributable cost shares could be said to reflect the degree to which individual products “benefitted” from specific processing activities, and thus allocating institutional costs in the same proportion as attributable costs would likewise fairly reflect the “benefits” each product received from the incurrence of the costs of that activity. Postal Service Comments at 38-39.

The 1999 bill also contained a provision setting forth “special circumstances” under which the equal markup formula could be adjusted. *Id.* at 37. Specifically, it provided that:

(b) Adjustment for Special Circumstances.--The Postal Regulatory Commission may, by rule, and in order to ensure that ratios under this section appropriately compensate for any significant and objective differences in the nature and composition of costs attributable to competitive and noncompetitive products, respectively, provide for the exclusion of such costs attributable as the Commission considers to be *uniquely or disproportionately associated* with either category of products.

Id. at 37 (citing Postal Modernization Act of 1999 § 3744(b) (emphasis added)). The Postal Service contends that “[a]bsent any contrary explanation, this provision plainly constitutes the origin of the exact same ‘uniquely or disproportionately associated’ phrase that now appears as part of subsection 3633(b).” *Id.*

⁸⁴ *Id.* at 34 (citing Postal Modernization Act of 1999, H.R. 22, 106th Congress (1999)).

⁸⁵ *Id.* (citing Postal Modernization Act of 1999 § 3744(a)).

According to the Postal Service, during the period that this draft legislation was being considered, the Postal Service was developing, and in some cases, implementing, plans to initiate separate processing activities that would be specifically dedicated to products that are now classified as Competitive. *Id.* at 39-40. Hence, the purpose of the “special circumstances” provision was to exclude the attributable costs relating to these activities from the equal markup ratio calculation. *Id.* at 40. To the extent that such operations were dedicated solely to Competitive products, the costs associated with them would have been wholly attributable, but including them with other attributable costs for purposes of calculating the equal markup ratio would have defeated the ratio’s purpose, as it would have caused the attributable cost shares to no longer fairly reflect the relative “benefits” from the Postal Service’s shared infrastructure being received by Competitive products as compared to Market Dominant products. *Id.* at 40-41. While historically it was only with respect to Competitive products that the Postal Service seriously contemplated implementing dedicated operations (and those plans were subsequently abandoned), the Postal Service asserts that the “uniquely or disproportionately associated” language would have equally worked to exclude any costs associated with dedicated Market Dominant operations, if such operations had ever been implemented. *Id.* at 45-46.

The Postal Service characterizes the overall “equal markup” approach as a parallel appropriate share framework to that enacted later in the PAEA, albeit one in which the appropriate minimum was set directly by statutory formula, rather than as judgmentally determined by the Commission. *Id.* at 49. The Postal Service emphasizes that the “special circumstances” provision was not concerned with reexamining how specific costs were classified (*i.e.*, as attributable or institutional), or with creating an additional category of costs in addition to attributable costs and institutional costs. *Id.* at 48. Rather, it was focused only on excluding attributable costs that were associated with dedicated operations from the “equal markup” calculation. *Id.* Furthermore, the

primary function of the “equal markup” approach would have been to reduce the allocation of institutional costs to Competitive products, not to increase it. *Id.* at 49-50.

As the Postal Service explains, by 2002 postal reform bills had discontinued the “equal markup” approach to institutional cost allocation, replacing it with a requirement that Competitive products either make a “reasonable contribution” to institutional costs (the approach taken in House versions of postal reform), or that Competitive products cover “their share” of institutional costs (the approach taken in Senate versions of postal reform).⁸⁶ Existing 39 U.S.C. § 3633(b), including the “uniquely or disproportionately associated” language that was ultimately enacted as part of the PAEA, first appeared in a Senate postal reform bill in 2005.⁸⁷

The Postal Service emphasizes that 39 U.S.C. § 3633(b), by its very terms, had no effect until 5 years after the PAEA was enacted, at the time of the Commission’s first required periodic review of the appropriate share. Postal Service Comments at 52. Hence, to the Postal Service, the provision “was intrinsically focused on subsequent *changes* in circumstances that might have some bearing on what would be an appropriate share[;] [o]therwise, the specified factors would have been required to be considered as part of the initial regulatory consideration.” *Id.* (emphasis in original). The Postal Service identifies two sources of change that it believes the drafters of the PAEA would have logically been concerned with—external changes (*i.e.*, those involving competitors and the market); and internal changes (*i.e.*, those involving the Postal Service’s internal structure and its operations). *Id.* With respect to external changes, the Postal Service asserts that the “prevailing competitive conditions in the market” “encapsulate[] how the market for Competitive products might have evolved

⁸⁶ *Id.* at 50-51 (citing PAEA, H.R. 4970 (107 Cong, 2nd Sess.), 39 U.S.C. § 3633 (June 20, 2002); PAEA, S. 2468 (108 Cong, 2nd Sess.), 39 U.S.C. § 3633 (August 25, 2004)).

⁸⁷ Postal Service Comments at 51-52 (citing PAEA, S. 662 (109 Cong, 1st Sess.), 39 U.S.C. § 3633(b) (March 17, 2005)).

since any prior assessment of the appropriate share.” *Id.* With respect to internal changes, the Postal Service asserts that in as much as:

[O]ne of the more fundamental and prominent features of the [PAEA] was the bifurcation of postal products into Competitive and Market Dominant categories that did not exist under the [PRA], with substantial differences in treatment afforded each category[.] . . . no one had any clear idea of whether or how postal operations five or ten years down the road might have been restructured in response to the full array of the new law’s changes to the Postal Service’s authority and obligations[.]

Id. at 53. At the same time, however, “from the previous experience with the aborted ‘equal markup’ approach, there was undeniable awareness that considering the issue of institutional cost coverage by Competitive products might to some degree require consideration of whether activities generating those institutional costs were intended to handle all types of mail or were designed specifically for one particular category.” *Id.* at 53-54. Hence, “in addition to consideration of changes in market circumstances, the five-year reviews are also intended to consider potential changes in operational circumstances relating to the effects of activities dedicated to Competitive products.” *Id.* at 54. The Postal Service states:

[T]he purpose of [the ‘uniquely or disproportionately associated’ language] is functionally the same as the similarly-worded adjustment provision in the [1999 bill] with respect to the minimum share established under the ‘equal markup’ rule: to compel recognition that the existence of operations dedicated to Competitive products are (at least potentially) relevant to determinations of what may be an appropriate minimum share.

Id.

The Postal Service spotlights two differences in the 1999 bill containing the equal markup requirement with the provision that was later codified in 39 U.S.C. § 3633(b).

Id. First, the 1999 bill’s version of the provision was expanded from consideration of “attributable costs” that are uniquely to disproportionately associated to consideration of “any costs” that are uniquely or disproportionately associated. *Id.* at 54-55. Second, the 1999 bill’s version of the provision was narrowed to focus only on costs associated

with Competitive products, rather than costs associated with either Competitive or Market Dominant products. *Id.* The Postal Service speculates that “since the appropriate share exercise in this portion of chapter 36 is directed solely at Competitive products, the need to consider comparable circumstances as applicable to Market Dominant products would be minimal.” *Id.* at 55. Furthermore, “the relevant prior experiences, buttressed by the new provisions of the PAEA regarding Competitive products, made it far more likely that any operational innovations would relate to the segregation of selected Competitive products from routine operations, as opposed to any corresponding efforts to segregate Market Dominant products.” *Id.* at 56.

The Postal Service also notes two new elements in the final clause of 39 U.S.C. § 3633(b) relative to the 1999 postal reform bill containing the equal markup requirement. *Id.* One is the addition of the phrase “the degree to which.” *Id.* According to the Postal Service:

With the addition of this phrase, the clause does not instruct the Commission to consider ‘associated costs’ directly, but rather requires consideration of ‘the degree to which’ there may be such associated costs Consequently, it is not the individual instances of ‘associated’ costs that require examination during the periodic review, but rather the cumulative effect of potential changes in aggregate ‘associated’ costs.

Id. The Postal Service explains that:

In the aggregate, consideration of ‘the degree to which’ there are associated costs was intended to be used as a barometer to gauge whether the operational structure used to handle Competitive products was materially changing over time towards dedicated operations for competitive products[,] . . . [in which case] the Commission would then need to consider any such structural changes when reevaluating what, if anything, constituted an appropriate share of institutional costs, just as it would be required to consider changes in the prevailing competitive market conditions.

Id. at 56-57.

The second new element of the “uniquely or disproportionately associated” provision that the Postal Service identifies relative to the 1999 postal reform bill containing the equal markup requirement is the requirement that the Commission need only “consider” the “degree to which any costs are uniquely or disproportionately associated with any competitive products,” as one among other “relevant circumstances.” *Id.* at 57. According to the Postal Service:

In the 1999 draft, a very rigid and mechanistic procedure was mandated—the Commission would have been compelled to apply the ‘equal markup’ ratio, and application of the special circumstances adjustment would have been equally mechanistic[;] [i]n contrast, in current section 3633(b), the Commission must give this factor consideration, but . . . the Commission is left with broad discretion in terms of what other factors it may deem also to be relevant, and what weight to give this consideration, as well as other potentially competing factors.

Id. As a result, “[t]he overall process is . . . much more subjective and qualitative in nature, with broad discretion vested in the Commission.” *Id.*

Taking all the foregoing into consideration, the Postal Service expresses its understanding of the purpose of the “uniquely or disproportionately associated” phrase in 39 U.S.C. § 3633(b) as follows:

Having previously determined an “appropriate share” of institutional costs to be borne by Competitive products collectively, the Commission must review that determination every five years. While required to consider changes in “all relevant circumstances” when deciding to retain, modify, or eliminate the requirement as previously established, one consideration that the Commission must consider is “the degree to which any costs are uniquely or disproportionately associated with any competitive products.” In doing so, the Commission is expected to consider the degree to which any new activities have been established as dedicated operations for Competitive products during the intervening five years (or perhaps whether any previous such dedicated operations have been withdrawn). If no indications of sufficient evolution in the overall operational structure are detected, no further consideration is required. On the other hand, if warranted by evidence of sufficient new activities, this re-examination may

encompass consideration of how such activities impact whether all products are being handled in operations generating institutional costs to the same extent as they did previously, and whether that merits any adjustment to the appropriate share, most likely to reduce it.

As with any activities, there will be accrued costs generated by these operations, and application of standard postal costing principles as they have evolved since the PAEA would attribute most or all of those costs from dedicated operations to Competitive products (depending, in part, on the extent to which any Market Dominant products might be incidentally handled as well), and to identify no institutional costs. Assuming that some of these new dedicated operations are identified during the five-year review, the task then facing the Commission is to consider the degree to which the mix of attributable and institutional across all postal activities might be sufficiently affected by the addition of the costs relating to the new dedicated activities (*i.e.*, those “uniquely or disproportionately associated with any competitive products”) as to alter the prior determination of what constitutes the appropriate share. The Commission, in other words, would need to assess whether, in the aggregate, the incidence of “associated” costs pools in the aggregate remained static, or changed to only a minor degree, or instead changed to a sufficient degree to trigger an adjustment. A sufficient change in the degree to which costs are accrued in operations dedicated to Competitive products could prove to be a harbinger of structural change so fundamental as to be potentially relevant to the evaluation of the “appropriate” share.

Id. at 57-59.

The past orders in this docket stated that the Commission was unable to confirm the Postal Service’s assertions regarding the legislative intent behind the “uniquely or disproportionately associated” phrase because nothing in the PAEA’s legislative history corroborated the Postal Service’s assertions concerning the drafters’ intent. Order No. 4963 at 148; Order No. 6043 at 55 n.91. The Postal Service now “acknowledges that its earlier . . . comments . . . did not do full justice to . . . [the Postal Service’s argument].” Postal Service Comments at 60. Nevertheless, having now fully articulated its interpretation of the “uniquely or disproportionately associated” phrase, the Postal Service contends that “[t]aking explicit account of how the same statutory language was

intended to function in the earlier version of the bill constitutes a reasonable interpretation of the last clause of [s]ection 3633(b).”⁸⁸

In terms of applying its preferred interpretation of the “uniquely or disproportionately associated” phrase, the Postal Service explains that since the PAEA was enacted, postal operations have not, in fact, evolved towards more dedicated operations for Competitive products; generally, Competitive products are still handled in integrated operations in which they are commingled with Market Dominant products. Postal Service Comments at 62-63. Thus, “there is not any basis to conclude that there have been material changes in the degree to which Competitive products are handled in dedicated operations.” *Id.* at 63. The Postal Service identifies Sunday delivery of Competitive products (the costs of which are wholly attributed to Competitive products) as a potentially relevant activity to be considered under the “uniquely or disproportionately associated” provision, but the Postal Service asserts that Sunday delivery should not affect the Commission’s determination as to the appropriate share because Sunday delivery has not meaningfully reduced the presence of Competitive products in commingled processing operations on the other 6 days of the week, and hence constitutes only a “minor change” in the degree to which accrued costs are “associated” with Competitive products. *Id.* at 63-65.

⁸⁸ *Id.* at 61-62 (citing 2A Sutherland Statutory Construction § 48.3 (7th ed.) (“As with all legislative history, courts generally turn to a law’s pre-enactment history to discover its purpose, or object, or the mischief at which it was aimed, when the statute’s language is inadequate to reveal legislative intent.”); *Id.* § 48.4 (“Events immediately prior to the time an act becomes law can be a useful source to learn about legislative intent. Indeed, the first extrinsic aid courts usually consult to interpret an ambiguous statute is a measure’s history during the enactment process, from its introduction in the legislature to its final validation.”))

2. Commission Analysis

With respect to ASL's comment that Order No. 6043's interpretation of the "uniquely or disproportionately associated" phrase was "unduly favorable to UPS" (see ASL Reply Comments at 16), the Commission clarifies what appears to have been a misunderstanding by ASL regarding the Commission's interpretation. ASL asserts that "[t]he section 3633(b) standard does not require consideration of *all* costs that might be associated with Competitive products, only those that are "*uniquely or disproportionately associated*" with Competitive products." ASL Reply Comments at 16 (emphasis in original). As instructed by the court, the Commission considers all accrued costs (that is, both institutional and attributable costs) to determine if any are potentially "uniquely or disproportionately associated" with Competitive products. See Order No. 6043 at 71 (citing *UPS II*, 955 F.3d at 1045, 1051)). To be clear, the Commission's interpretation of the "uniquely or disproportionately associated" phrase is that to be relevant to the Commission's appropriate share determination, a cost must be "*uniquely or disproportionately associated*," as set forth under 39 U.S.C. § 3633(b) rather than merely associated with Competitive products. See *id.* at 51-52, 72-73.

With respect to the Postal Service's proposed alternative interpretation of the "uniquely or disproportionately associated" phrase, the Commission continues to find that while the Postal Service's proposed interpretation is plausible, there is no way to verify that the Postal Service's interpretation is what the drafters of the PAEA intended. Although the "uniquely or disproportionately associated" language in 39 U.S.C. § 3633(b) is identical to the language used in H.R. 22 in 1999, the "equal markup" requirement from the 1999 bill was a very different approach to institutional cost allocation from what was ultimately enacted in the final version of the PAEA in December 2006.⁸⁹ The Commission cannot verify that the "uniquely or

⁸⁹ Compare Postal Service Comments at 34 (quoting Postal Modernization Act of 1999 § 3744(a)), with 39 U.S.C. § 3633(b).

disproportionately associated” phrase was intended to play the same role in the final enacted version of the PAEA that it would have played in the 1999 bill. No legislative history is associated with either H.R. 22 in 1999 (the first appearance of the phrase “uniquely or disproportionately associated”) or S. 662 in 2005 (its reappearance before the PAEA’s enactment).

Because the Postal Service’s interpretation is circumstantial and speculative, based primarily on the use of the same phrase in two otherwise very different provisions in different versions of postal reform bills, one of which predated the PAEA by nearly a decade, the Commission is unable to adopt the Postal Service’s interpretation. Instead, the Commission has interpreted the “uniquely or disproportionately associated” phrase based on its plain text in conjunction with the text, structure, and purpose of 39 U.S.C. § 3633 and the PAEA more generally.⁹⁰ Thus, consistent with the court’s instructions, the Commission has reasonably considered both institutional and attributable costs to determine if any are potentially “uniquely or disproportionately associated” with Competitive products. See Order No. 6043 at 71 (citing *UPS II*, 955 F.3d at 1045, 1051)).

V. COMMISSION ANALYSIS OF ALL RELEVANT CIRCUMSTANCES

“In making its determination [whether to retain, modify, or eliminate the appropriate share], the Commission shall consider all relevant circumstances, including the prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products.” 39 U.S.C. § 3633(b). Section V.A., *infra* summarizes prior Commission findings and addresses

⁹⁰ *Petit*, 675 F.3d at 781 (At *Chevron* step one, “a court must “exhaust the traditional tools of statutory construction to determine whether Congress has spoken to the precise question at issue[.] . . . [which] include examination of the statute’s text, legislative history, and structure, as well as its purpose.” (quoting *Bell Atl. Tel. Cos. v. FCC*, 131 F.3d 1044, 1047 (D.C. Cir. 1997) (internal marks omitted)).

comments received related to the Commission's application of the "the degree to which any costs are uniquely or disproportionately associated with any competitive products" to all of the Postal Service's accrued costs (*i.e.*, both attributable and institutional costs). 39 U.S.C. § 3633(b). Section V.B., *infra* summarizes prior Commission findings and addresses comments received related to how the Commission's dynamic formula-based approach captures "all relevant circumstances, including the prevailing competitive conditions in the market." 39 U.S.C. § 3633(b).

For the reasons discussed below, the Commission readopts its dynamic formula-based approach as presented in Order No. 6043.

A. Uniquely or Disproportionately Associated Costs

1. Background

As required on remand, Order No. 6043 fully articulated the Commission's consideration of the phrase "the degree to which any costs are uniquely or disproportionately associated with any competitive products" by considering all costs that the Postal Service accrues in the course of business, *i.e.*, costs classified as either attributable or institutional.⁹¹

⁹¹ See Order No. 6043 at 72; 39 U.S.C. § 3633(b). An attributable cost is one that can be linked to individual products or groups of products through reliably identified causal relationships between cost and product. See Order No. 6043 at 72; 39 U.S.C. § 3631(b) ("[T]he term 'costs attributable', as used with respect to a product, means the direct and indirect postal costs attributable to such product through reliably identified causal relationships."). Attributable costs are determined for Competitive products and groups of Competitive products, as well as for Market Dominant products and Market Dominant products by class. See Order No. 6043 at 72 n.120; 39 U.S.C. § 3622(c)(2). Institutional costs are residual costs that cannot be attributed to postal products through reliably identified causal relationships and are calculated by removing attributable costs from total accrued costs. Order No. 6043 at 72.

a. Attributable Costs

All costs that are attributed to Competitive products at both the individual product and group level are uniquely or disproportionately associated with Competitive products.⁹² This is because attributable costs exhibit reliably identified causal relationships to products, which is a narrower standard that is subsumed by the broader “uniquely or disproportionately associated” phrase appearing in 39 U.S.C. § 3633(b). *Id.*

As instructed by the court, the Commission then considered whether these attributable costs (which also are “uniquely or disproportionately associated with any competitive products” pursuant to 39 U.S.C. § 3633(b)) are relevant to setting the appropriate share pursuant to 39 U.S.C. § 3633(b). *See UPS II*, 955 F.3d at 1051; Order No. 6043 at 75-80. In its analysis, the Commission first explained that the three provisions of 39 U.S.C. § 3633(a) serve to implement different (albeit interrelated) price floors relating to the Postal Service’s Competitive products.⁹³ The Commission then illustrated the operation of these price floors. *See id.* at 77, Table VI-1. The Commission explained that because individual product and group level costs must be covered *before* any contribution toward institutional costs can occur, no further added

⁹² Order No. 6043 at 8, 74. At the individual product level, these costs include product-level volume-variable costs, product-specific costs, and those inframarginal costs that can be calculated as part of a product’s incremental cost. *Id.* at 74. These costs are attributed to individual Competitive products pursuant to 39 U.S.C. § 3633(a)(2). *Id.* At the group level, these costs include costs caused by multiple Competitive products or Competitive products collectively, *i.e.*, group-specific costs and group-level inframarginal costs that can be calculated as part of incremental costs pursuant to 39 U.S.C. § 3633(a)(1). *Id.*

⁹³ Order No. 6043 at 75. Specifically, 39 U.S.C. § 3633(a)(2) represents the price floor for each individual Competitive product by requiring that the prices set for each individual Competitive product must generate revenue that covers the costs attributable to that individual Competitive product. *Id.* Similarly, 39 U.S.C. § 3633(a)(1) represents a price floor for Competitive products collectively. *Id.* Additionally, 39 U.S.C. § 3633(a)(3) represents another price floor for Competitive products collectively because the prices set for Competitive products collectively must be marked up high enough to generate revenue above and beyond the costs attributable to Competitive products at the individual product and group level to also cover an appropriate share of the Postal Service’s institutional costs. *Id.* at 75-76.

protection from the appropriate share requirement of 39 U.S.C. § 3633(a)(3) is necessary to ensure that Competitive products cover attributable costs. *Id.* at 78.

Next, the Commission explained that any attempt to account for attributable costs by adjusting the Commission's formula would essentially double-count⁹⁴ them in a way that is unnecessary, economically unsound, and would be harmful to the Postal Service and its Competitive product business.⁹⁵ Due to competition, if prices were set significantly higher in an attempt to satisfy a requirement to cover attributable costs twice, volumes would decrease by an amount that would be difficult to predict. *Id.* at 79, n.123. Such volume decreases would, in turn, result in lower attributable costs, but also lower revenues. *Id.* As a result, the Commission stated that these changes and the resulting impacts on the Postal Service's market share would also affect the inputs into the Commission's formula for calculating the appropriate share. *Id.* The Commission noted that these attributable costs are not ignored in its review pursuant to 39 U.S.C. § 3633(b) and are indirectly relevant to setting the appropriate share because they are used in the Commission's dynamic formula-based approach.⁹⁶

⁹⁴ Double-counting of these attributable costs would occur first through attribution and then again through the appropriate share requirement. *Id.* at 78.

⁹⁵ Incorporating attributable costs in their entirety (again) or by some lesser amount "would result in the Postal Service being forced to set prices that send inefficient pricing signals related to the Postal Service's Competitive products." *Id.*

⁹⁶ Costs attributable to Competitive products are used to calculate the Competitive Contribution Margin (CCM), one of the two components that make up the formula. *See id.* at 79. The CCM measures the change in the Postal Service's absolute market power for any given fiscal year by calculating the difference between the total attributable costs of producing the Postal Service's Competitive products collectively, and the amount of revenue the Postal Service can realize from Competitive products collectively. *Id.*

b. Institutional Costs

The Commission determined that attempting to allocate institutional costs in its review of the minimum contribution requirement would lack justification from an economic and cost-accounting perspective.⁹⁷ Because there is no discernable relationship between institutional costs and any product or group of products, any allocation of these costs would be arbitrary, and therefore attempting to relate institutional costs and Competitive products is neither meaningful nor relevant to the Commission's determination of the appropriate share. *Id.* at 83.

Institutional costs contain some discrete fixed costs that are easily identifiable, but they make up only a small portion of the Postal Service's institutional costs.⁹⁸ Aside from those discrete fixed costs, the remainder of costs classified as institutional are a mixture of fixed costs and costs that can be described as unattributed inframarginal costs.⁹⁹ This mixture of costs cannot be organized into distinct amounts because there is no way to determine which portion of institutional costs are unattributed inframarginal

⁹⁷ *Id.* at 83. Costs classified as institutional are a residual category of costs that remain after costs have been attributed at the product- and group-levels. *See id.* at 80. These residual costs consist of a mixture of several kinds of costs, most of which are not separable from one another. *Id.*

⁹⁸ *Id.* For example, Cost Segment 17—Research and Development includes “costs for materials, equipment, and contract services relating to research and development.” FY21 Summary Descriptions, file “CS17-21.docx,” at 17-1. Cost Segment 7—City Delivery Carriers, Street Activity includes costs from Cost Component 54 (Network Travel) which are the costs associated with the time spent traveling between delivery sections or certain pick-up and drop-off points for Special Purpose Routes (SPRs). FY21 Summary Descriptions, file “CS07-21.docx,” at 7-3.

⁹⁹ Order No. 6043 at 81. Inframarginal costs are the difference between the incremental cost of a product (or group of products) and the volume-variable cost of that product, putting aside product-specific costs. *Id.* at 27. These costs are variable and while some can be attributed to products or groups of products, others cannot. *See id.* at 81, n.129. Table VI-2 provides an example of a cost segment that contains cost components with discrete fixed institutional costs as well as cost components where the costs in the institutional category are a mixture of fixed and unattributed inframarginal. *See id.* at 82, Table VI-2. The institutional costs are labeled as “other costs” in the table, indicating that these are the costs that remain after the attributable portion of costs has been identified. *See id.*

costs, *i.e.*, the inframarginal costs not calculated as part of incremental costs.¹⁰⁰

Furthermore, the Commission noted that the inframarginal costs that are institutional are, *in part*, related to the provision of both Competitive and Market Dominant products, due to the economies of scale and scope from their joint production.¹⁰¹

There is no way to reasonably separate a cost component's institutional costs into unattributed inframarginal costs and fixed costs categories and then further segregate the unattributed inframarginal costs into those that are *meaningfully* related to the provision of Competitive products and those that are *meaningfully* related to the provision of Market Dominant products. *Id.* at 84. As such, the Commission concluded that there are no uniquely or disproportionately associated costs in institutional costs. *Id.* at 7.

If the Commission tried to apportion such institutional costs to products, it would be forced to assign an arbitrary share or proportion of the Postal Service's total institutional costs to Competitive products and require them to cover that amount as part of the price floor represented in 39 U.S.C. § 3633(a)(3). *Id.* at 85. It noted that such an exercise is a form of fully distributed costing as it relates to the Postal Service's Competitive products and provided several reasons that such an exercise would be economically unsound. *See id.* at 85-92. In addition, in Tables VI-5 through VI-7, the Commission illustrated how the arbitrary allocation of institutional costs can cause distortions related to product profitability, when allocating costs equally among products,

¹⁰⁰ *Id.* at 81. To identify which portion of institutional costs are unattributed inframarginal costs, the Commission indicated that it would need to be able to estimate total inframarginal costs, which would require a reliable estimate not just for marginal costs, but also for the Postal Service's total variable costs. *Id.* at 84. However, no viable estimate for the total variable costs of the Postal Service exists because as a multi-product firm, variable costs that are classified as institutional are accrued simultaneously with fixed costs that are classified as institutional. *Id.*

¹⁰¹ *Id.* at 82, 84. These costs are caused by the existence of a system in which both Market Dominant and Competitive products are handled *simultaneously* and consist of the portion of costs that cannot be separately identified and linked to either Market Dominant or Competitive products. While it is true that the provision of Competitive products relies on the existence of this system; it is equally true that the provision of Market Dominant products relies on the existence of this system. *Id.* at 83.

or based on relative shares of volume and attributable costs. *See id.* at 89-90, Tables VI-5-VI-7. Thus, it noted that, with no rational basis for preferring one allocation method over another, the arbitrary selection of cost assignment can create vastly differing impressions of the financial viability of the products, which is data the Postal Service uses to make decisions related to pricing, among other things. *Id.* at 90. The Commission further noted that such an occurrence could force the Postal Service to cease offering products that are, in actuality, improving its finances by helping to cover institutional costs, or alternatively, to raise the prices of those products to an unsustainable level. *Id.* at 91.

The Commission also discussed the potential risk of creating a price umbrella if the 39 U.S.C. § 3633(a)(3) price floor were set too high. *Id.* at 61, 91-92. Doing so would shield competitors from full price competition and distort fair competition at the expense of consumers. *See id.* The Commission noted such a result would be contrary to the purpose of the governing statute, including 39 U.S.C § 3633(a)'s aim of preventing unfair competition, 39 U.S.C. § 3633(b)'s aim of reviewing the minimum contribution, and the overall pro-competitive aims of the PAEA's scheme for regulating Competitive products. *Id.* at 92. The Commission also discussed UPS's argument on appeal that the Commission did not consider whether its formula-based approach would prohibit the Postal Service from setting prices artificially low. *Id.* (citing UPS Brief at 40). The Commission confirmed that no evidence indicated that the Postal Service has engaged in anticompetitive pricing, nor was the Commission persuaded that the Postal Service may engage in anticompetitive pricing in the future. *Id.* at 92-94. Furthermore, the Commission explained that because its dynamic formula accounts for absolute market power and changes in market position, if the Postal Service were to derive some

benefit from costs being classified as institutional, the formula would account for any benefit and the appropriate share would increase.¹⁰²

c. Conclusion

For the reasons discussed above, the Commission found that all costs that are meaningfully related to the provision of Competitive products are already attributable to Competitive products under the Commission's current cost attribution principles. *Id.* at 74. It also concluded that no meaningfully related costs exist within Postal Service institutional costs.¹⁰³ It further found that the above-described harms from arbitrarily allocating institutional cost is much more likely than the possibility of the Postal Service engaging in anticompetitive pricing because of not allocating institutional costs. Order No. 6043 at 92.

No comments challenged the Commission's conclusion that all costs that are attributed to Competitive products at both the individual product and group levels are "uniquely or disproportionately associated" with Competitive products. This is because attributable costs reflect reliably identified causal relationships (see 39 U.S.C. § 3631(c)), which is a narrower standard than the broader "uniquely or disproportionately associated" phrase appearing in 39 U.S.C. § 3633(b).¹⁰⁴ Commenters discussed the following topics relating to the Commission's application of the requirement to consider "the degree to which any costs are uniquely or disproportionately associated with any competitive products" phrase appearing in 39

¹⁰² *Id.* at 94. The Commission retains the authority to revisit the appropriate share requirement at any time to reassess the elements of 39 U.S.C. § 3633(b), especially should the Postal Service change its pricing behavior or contribution to institutional costs begin to decline. *Id.* at 94-95.

¹⁰³ *Id.* at 74. This finding specifically responds to the court's question "[a]re some of the Postal Service's institutional costs – and especially its unattributed inframarginal costs – still *related in some meaningful way to competitive products*, even if those costs cannot be attributed under § 3633(a)(2)?" *UPS II*, 955 F.3d at 1045 (emphasis added).

¹⁰⁴ See Section IV.C.2., *supra*; Order No. 6043 at 74. See also *UPS II*, 955 F.3d at 1049.

U.S.C. § 3633(b): whether the Commission adequately “considered” costs uniquely or disproportionately associated with Competitive products; whether the appropriate share is necessary in order to ameliorate an alleged deficit left by the use of the incremental costs test for cost attribution; the appropriateness of incorporating attributable costs without some level of double-counting; whether any costs uniquely or disproportionately associated with Competitive products exists within institutional costs; whether the Commission adequately addressed unattributed inframarginal costs; the appropriateness of the Commission’s use of sound economic measurement; and the arbitrary allocation of costs to Competitive products and Market Dominant products.

2. The Commission Considered the Degree to Which Any Costs are Uniquely or Disproportionately Associated with Any Competitive Products

a. Comments

UPS quotes the court’s statement that “[o]n remand, the Commission must consider all costs uniquely or disproportionately associated with competitive products in setting the appropriate share, even if it has already accounted for those costs under § 3633(a)(1) and (a)(2).” UPS Comments at 47 (quoting *UPS II*, 955 F.3d at 1051) (emphasis omitted). UPS argues that the Commission’s “continued refusal to consider these costs . . . conflicts directly with the D.C. Circuit’s mandate.” *Id.* UPS further contends that the Commission’s rationale for “ignoring these costs does not withstand scrutiny.” *Id.*

UPS also disagrees with the Commission’s statement that its dynamic formula implicitly considers these costs because Competitive product attributable costs are used to calculate the CCM. *Id.* at 47-48. UPS contends that the Commission’s explanation “distorts how the formula actually works.” *Id.* at 47. It argues that the CCM is not used on its own, and instead considers only the annual change in that variable, which means the attributable costs themselves are not considered. *Id.* at 48. UPS adds that “the only

supposed consideration of costs uniquely or disproportionately associated with competitive products provided by the Commission's formula—to the extent they are reflected in costs attributed to competitive products—is that an *increase* in such costs would mean a *lower* price floor for competitive products,” which “conflicts with what Congress intended.” *Id.* (emphasis in original).

b. Commission Analysis

In Order No. 6043, the Commission found that all costs that are attributed to Competitive products at both the individual product and group level are uniquely or disproportionately associated with Competitive products. Order No. 6043 at 74. No participant submitted comments challenging this conclusion.

The Commission further explained that the Postal Service's Competitive products are already responsible for covering those costs through the collective price floor established by 39 U.S.C. § 3633(a)(1) and the sum of the individual product price floors established by 39 U.S.C. § 3633(a)(2). *Id.* at 72. Moreover, the Commission explained that its calculation of the price floor set by 39 U.S.C. § 3633(a)(3) already includes those costs (and in fact, the price floor set by 39 U.S.C. § 3633(a)(3) exceeds this amount).¹⁰⁵ As a result, the Commission found that no further added protection from the appropriate share requirement of 39 U.S.C. § 3633(a)(3) was necessary to ensure that Competitive products cover attributable costs. *Id.* at 78.

Despite the Commission's lengthy explanation, UPS views the Commission's conclusion related to these specific costs as a failure to “consider” uniquely or disproportionately associated costs. *See, e.g.*, UPS Comments at 47. It appears UPS misinterprets the requirement to “consider” as meaning “include” and thus interprets 39 U.S.C. § 3633(b) and the court as directing the Commission to *include* any costs

¹⁰⁵ *Id.* To support its conclusions, the Commission provided a lengthy discussion of the price floors set by 39 U.S.C. § 3633(a) and their requirements. *See id.* at 74-80. *See also id.* at 77, Table VI-1.

uniquely or disproportionately associated costs with Competitive products when determining appropriate share even if those costs are already attributed to Competitive products and included in the price floors established by 39 U.S.C. § 3633(a)(3). However, as the Commission explained in Order No. 6043, the requirement to “consider” all relevant circumstances means “to think about carefully,” or “to take into account.”¹⁰⁶ This requirement does not mean that the Commission must “adhere to,” “be bound by,” or “follow” any particular relevant circumstance in reaching its determination. *Id.* (citing *Bruce*, 285 F.3d at 73).

Contrary to UPS’s claims, the court endorsed the Commission’s interpretation of this requirement. The court expressly repudiated the notion that the Commission *must include* uniquely or disproportionately associated costs that are attributed to Competitive products as part of its appropriate share determination and that the Commission must adjust the 39 U.S.C. § 3633(a)(3) price floor if the Commission found any costs uniquely or disproportionately associated with competitive products, stating:

In sum, the Commission must address the issues highlighted above before we can say whether its formula-based approach to determining the appropriate share under § 3633(a)(3) is permissible and reasonable. On remand, the Commission might decide to revise its judgment regarding the “appropriate share” under § 3633(a)(3). Indeed, at oral argument, counsel for the Commission conceded that the “floor” established under § 3633(a)(3) might need to be adjusted if the Commission found any costs uniquely or disproportionately associated with competitive products. Tr. Of Oral Argument at 49-50. It is also possible, however, that the Commission might decide against revising its bottom-line judgment, given the other factors the Commission must consider under § 3633(b) and the latitude that the text affords the Commission in making a final determination.

¹⁰⁶ Order No. 6043 at 50 (citing Merriam-Webster Dictionary, available at <https://www.merriam-webster.com/dictionary/consider>, definitions 1.a.-b.).

We take no position on this matter. It is not for this court to say that the Commission must account for costs in any specific way under § 3633(b) or that the Commission must make any particular ‘appropriate share’ determination under § 3633 (a)(3). Rather, the judgment of the court is that, on remand, the Commission must consider all the costs referenced under § 3633(b), as the Accountability Act clearly commands. And any decision that the Commission reaches regarding the meaning and application of § 3633(b) in connection with the “appropriate share” determination under § 3633(a)(3) must be consistent with the terms of the statute, must be comprehensible, and must otherwise satisfy the requirements of reasoned decision-making.

UPS II, 955 F.3d at 1051-52. Thus, the Commission finds that UPS’s interpretation is inconsistent with the text of 39 U.S.C. § 3633(b) and the court’s direction in *UPS II*.

The Commission “consider[ed]” these costs as required by 39 U.S.C. § 3633(b) and *UPS II*. The Commission applied its definition of a cost uniquely associated with Competitive products and a cost disproportionately associated with Competitive products to these costs that are attributable to Competitive products. See Order No. 6043 at 74. The Commission found that all costs that are attributed to Competitive products are also uniquely or disproportionally associated with those products. See *id.* As instructed by the court, the Commission then sought to determine whether these costs were relevant in setting the appropriate share. See *id.* at 75. As the Commission explained, those costs are already mathematically accounted for in the price floor of 39 U.S.C. § 3633(a)(3) and are thus not a relevant consideration to the amount that Competitive products should contribute to institutional costs. See *id.* at 75-78.

UPS does not dispute that these costs are already “covered” by the Postal Service’s Competitive products under 39 U.S.C. § 3633(a)(1) and (a)(2) and that Competitive product pricing already accounts for these costs. Nevertheless, UPS interprets 39 U.S.C. § 3633(b) “consider” as meaning “include” and it insists that these costs be included as part of the appropriate share (which is added as a margin of safety above and beyond the collective price floor set by 39 U.S.C. § 3633(a)(1) and thus recovered *again* by the Postal Service’s Competitive products). UPS provides no

evidence that would support its assertion that the inclusion of these costs in the appropriate share is consistent with the statutory purpose of 39 U.S.C. § 3633(a)(3). Nor does UPS explain why these costs are a relevant consideration to setting the appropriate share pursuant to 39 U.S.C. § 3633(b).

For these reasons, the Commission disagrees with UPS's assertion that it did not "consider" these costs and concludes that it fully considered these costs consistent with the court's instructions. It further concludes that its finding that costs already attributed to Competitive products are not directly relevant to setting the appropriate share remains valid.

The Commission disagrees with UPS's argument that the dynamic formula-based approach does not implicitly consider these costs via the CCM. See UPS Comments at 47. First, the Commission reiterates that the 39 U.S.C. § 3633(a)(3) price floor includes all costs attributed to Competitive products pursuant to 39 U.S.C. § 3633(a)(1) and (a)(2), plus the Commission-determined appropriate share of the Postal Service's institutional costs. See Order No. 6043 at 74-80. Given their role as the mathematical base for the 39 U.S.C. § 3633(a)(3) price floor, counting them again (as proposed by UPS) would be unnecessary and inappropriate. See *id.* Second, these costs are also used to calculate the CCM. *Id.* at 79. The CCM, which is one of the two components that make up the formula to determine the appropriate share, measures the change in the Postal Service's absolute market power for any given fiscal year. *Id.* Specifically, the CCM assesses market power based on the difference between the total attributable costs of producing the Postal Service's Competitive products collectively and the amount of revenue the Postal Service can realize from Competitive products collectively. *Id.*

UPS argues that increases in costs attributable to Competitive products are not properly accounted for because they would potentially lead to reductions to the CCM component and (by extension) the appropriate share amount produced by the dynamic formula. See UPS Comments at 48. However, increases in costs attributable to Competitive products would not reduce the 39 U.S.C. § 3633(a)(3) price floor because such costs serve as that price floor's mathematical base. See Order No. 6043 at 74-80. If Competitive products' attributable cost increased, *and all other terms are held constant*, it would indicate that the Postal Service does not have the market power to pass along the increased costs (in the form of higher prices to Competitive products). Thus, the Commission's dynamic formula-based approach appropriately considers "the prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products." 39 U.S.C. § 3633(b). By contrast, UPS provides no reasonable basis to support its contention that the Commission should assign even more weight to consideration of "the degree to which any costs are uniquely or disproportionately associated with any competitive products." *Id.*

As the hypothetical examples provided in Table V-1 illustrate, an increase to Competitive products' attributable costs (whether the increase is caused by newly generated attributable costs or costs moved from the Postal Service institutional costs, the percentage reduction to the appropriate share is the same under either scenario) leads to a net increase in the 39 U.S.C. § 3633(a)(3) price floor.

Table V-1
Hypothetical Scenarios: Collective 39 U.S.C. § 3633(a)(3) Price Floor

		Baseline	Scenario 1 \$1 Billion New Competitive Products Attributable Cost	Scenario 2 \$1 Billion from Institutional Cost to Competitive Product Attributable Cost
a	Competitive Product Revenue	\$34.0	\$34.0	\$34.0
b	Competitive Product Attributable Costs	\$21.0	\$22.0	\$22.0
c = a - b	Competitive Product Contribution	\$13.0	\$12.0	\$12.0
d = c ÷ a	Competitive Contribution Margin (CCM)	0.382	0.353	0.353
e	Institutional Costs	\$34.0	\$34.0	\$33.0
f	Competitive Growth Differential		0.00%	0.00%
g	Percentage Change in CCM		-7.69%	-7.69%
h	Appropriate Share (percentage)	10.1%	9.3%	9.3%
i = e x h	Appropriate Share (\$)	\$3.4	\$3.2	\$3.1
j = b + i	Total § 3633(a)(3) Floor	\$24.4	\$25.2	\$25.1

Note: Commission staff developed two hypothetical scenarios, applied corresponding changes to the inputs of the formula, and calculated the results.

For the reasons described above, the Commission has fulfilled the requirement to “consider all relevant circumstances, including the prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products.” 39 U.S.C. § 3633(b).

3. The Commission Considered the Potential Need for the Appropriate Share to Ameliorate an Alleged Deficit Left by the Use of the Incremental Costs Test

a. Comments

UPS asserts that the Commission must use the appropriate share requirement to ensure that Competitive products are not subsidized by Market Dominant products “given the very conservative test the Postal Service uses for determining which costs are [attributable, *i.e.*, the incremental cost test]” UPS Comments at 40. By

contrast, ASL explains that the incremental cost test is “simply the only correct way to determine the costs caused by a product or group of products, and the only economically sound way to apportion or assign costs to such products.” ASL Comments at 21-22 (citing Panzar Decl. at 24). Additionally, ASL asserts that the price floors under 39 U.S.C. § 3633(a)(1) and (a)(2) are sufficient alone to protect against cross-subsidization and predatory pricing. *Id.* at 26.

b. Commission Analysis

Throughout this docket and on appeal, UPS has repeatedly asserted that the Commission’s failure to adopt the UPS approach to the appropriate share fails to address deficits in cost attribution as instructed by the court. UPS Comments at 13-14, 40; UPS Brief at 31. However, this characterization is flawed because it is devoid of the proper context.

First, in both *UPS I* and *UPS II*, the court did not find that any deficit existed because of the Commission’s approach to cost attribution pursuant to 39 U.S.C. § 3633(a)(2). In *UPS I*, upon examining the Commission’s approach to cost attribution pursuant to 39 U.S.C. § 3633(a)(2), under which the Commission has established individual price floors for each Competitive product, the court stated that “UPS offers no reason to doubt that the Accountability Act’s prohibition on cross-subsidization, 39 U.S.C. § 3633(a)(1), and requirement that competitive products cover a share of institutional costs, *id.* § 3633(a)(3), will adequately ameliorate any competitive deficit left by the Commission’s approach to cost attribution.” *UPS I*, 890 F.3d at 1067. Similarly, in *UPS II*, the court observed that “[t]he court in [*UPS I*] recognized that, because the costs attributed test under § 3633(a)(2) is conservative, there may be institutional costs that are “uniquely or disproportionately associated with competitive products,” even though they cannot be said to stand in “reliably identified causal relationships” with them.” *UPS II*, 955 F.3d at 1051. In both cases, any potential competitive deficit was noted in reference to the individual price floors required by 39 U.S.C. § 3633(a)(2) not

(as UPS suggests) the higher collective price floor required by 39 U.S.C. § 3633(a)(1) (see UPS Comments at 40).

Second, in neither case did the court *require* that the Commission establish an appropriate share requirement to address any potential deficit. Rather, in both cases the court correctly understood that the price floor required by 39 U.S.C. § 3633(a)(1) played an integral role in addressing any *potential* competitive deficit left by the individual price floors required by 39 U.S.C. § 3633(a)(2) and in *UPS II*, the court instructed the Commission to fully articulate that connection. See *UPS I*, 890 F.3d at 1067; *UPS II*, 955 F.3d at 1051. As fully explained in Order No. 6043, in addition to establishing and determining the Postal Service's compliance with the individual Competitive product price floors as required by 39 U.S.C. § 3633(a)(2), the Commission established price floors for Competitive products collectively pursuant to 39 U.S.C. § 3633(a)(1) and (a)(3). See Order No. 6043 at 25-33. The Commission's calculation of the collective price floor required by 39 U.S.C. § 3633(a)(1) includes (and is higher than) the sum of the individual price floors required by 39 U.S.C. § 3633(a)(2). See *id.* at 8, 32. Then, as a margin of safety to protect against unfair competitive advantage, the Commission adds the appropriate share to the collective price floor required by 39 U.S.C. § 3633(a)(1). See *id.* The sum of the collective price floor required by 39 U.S.C. § 3633(a)(1) plus the appropriate share determined by the Commission equals the amount of the price floor applied to Competitive products collectively under 39 U.S.C. § 3633(a)(3). Overall, the prices floors set by 39 U.S.C. § 3633(a) require Competitive product prices to be set high enough to generate revenue that would meet or exceed costs attributable to Competitive products at the individual product and group levels and an appropriate share of the Postal Service's institutional costs. See *id.* at 7-8, 31 n.49, 32, 75-76. Thus, the collective price floors set by the Commission pursuant to 39 U.S.C. § 3633(a)(1) and (3) fully ameliorates any competitive deficit potentially left unaddressed by the individual price floors required by 39 U.S.C. § 3633(a)(2).

Nor are UPS's arguments concerning the occurrence of "subsidization" correct. See UPS Comments at 40. Incremental costs, which currently form the basis for attributable costs, represent the variable and fixed costs that would be eliminated if a product or group of products were discontinued, or, in other words, the total cost caused by the product or group of products. Order No. 6043 at 25. As defined pursuant to regulatory economics, a product or group of products is not being cross-subsidized if its revenues exceed its incremental cost.¹⁰⁷ Regardless, whether the Postal Service passes the incremental cost test at an enterprise-wide level (see UPS Reply Comments at 26-27), its Competitive product business does, which is the relevant inquiry under 39 U.S.C. § 3633(a)(1). The PAEA requires each postal product or group of products to recover the costs attributable to it, which the Commission verifies each year as part of its ACD pursuant to 39 U.S.C. § 3653(b)(1).

Furthermore, UPS's argument that "subsidization" can occur because of Competitive products failing to recover "their share" of institutional costs mistakenly assumes that such a thing exists. The Commission has already discussed the statutory interpretation flaws on which this mistaken assumption is based. See Sections IV.B.2., IV.C.2., *supra*. Moreover, as the Commission has explained, institutional costs are caused by all products collectively, and it is not possible to parse institutional costs to determine to what extent they are associated with either Market Dominant or Competitive products. Order No. 6043 at 81-84. There is no meaningful relationship

¹⁰⁷ ASL Comments at 20; see Panzar Decl. at 16. See also John C. Panzar, *The Role of Costs for Postal Regulation*, September 30, 2014, at 15 (2014 Panzar Report), available at <https://www.prc.gov/sites/default/files/reports/J%20Panzar%20Final%20093014.pdf> ("It is now standard in the regulatory economics literature that avoiding cross-subsidization means that the customers of each product (or group of products) pay more to the firm in revenues than the incremental cost of said product (or group of products).") (citing Viscusi, W. Kip; Joseph Harrington and John Vernon, (2005) *Economics of Regulation and Antitrust*, MIT Press, 4th Edition; Braeutigam, Ronald; "Optimal Policies toward Natural Monopolies," (1989) Chapter 30 in Richard Schmalensee and Robert Willig eds., *Handbook of Industrial Organization* Volume 2.).

between any current institutional costs and any products or groups of products, either Competitive or Market Dominant. *Id.*

As a general matter, the Commission notes that if UPS contends that any costs should be attributed to Competitive products, either individually or collectively, then UPS can petition the Commission to initiate a rulemaking proceeding in which UPS may propose an alternative costing methodology for the Commission to consider. Any interested party may petition the Commission to initiate proceedings (or the Commission may initiate a proceeding *sua sponte*) to consider proposals to change an accepted analytical principle. See 39 C.F.R. § 3050.11(a). These proceedings, which are filed in rulemaking dockets, are intended to improve the quality, accuracy, or completeness of data or data analysis in the reports the Postal Service submits each year to the Commission. *Id.* The Commission has long encouraged interested parties to bring such issues to the Commission's attention,¹⁰⁸ and a rulemaking docket is the appropriate forum to consider the types of allegations that UPS makes in this docket with respect to the Commission's costing methodologies. Specific types of costs raised by commenters are addressed in Section VII., *infra*.

4. The Commission Considered Incorporating Attributable Costs into the Minimum Contribution Requirement (With and Without Double-Counting)

a. Comments

UPS suggests the Commission could consider attributable costs without double-counting them by using the percentage of costs attributed to Competitive products compared to Market Dominant products as a reasonable estimate of the percentage of

¹⁰⁸ See, e.g., Docket No. RM2011-3, Order Closing Docket, November 3, 2015 (Order No. 2798) (closing a strategic rulemaking docket that identified and evaluated priorities to guide the Postal Service's studies and data collection efforts and improve the accuracy of the Postal Service's cost, volume, and revenue estimates used in its periodic reporting).

institutional costs that likewise should be covered by Competitive products. UPS Comments at 47. UPS claims that the PAEA requires such an action. *Id.*

ASL submits that the “Commission correctly concluded that ‘double-counting’ the same costs through their inclusion in the appropriate share determination would be an “economically unsound” approach.” ASL Comments at 29; ASL Reply Comments at 14. ASL further explains that incorporating attributable costs under the “discretionary” price floor of 39 U.S.C. § 3633(a)(3), “would likely distort competition.” ASL Comments at 29. ASL observes that “UPS agrees that ‘double-counting’ costs in two separate price floors . . . is improper” when it noted that the Commission could consider the costs without double-counting. ASL Reply Comments at 13-15. Similarly, Pitney Bowes agrees that the Commission’s conclusion that “‘double-counting’ the very same attributable costs as part of the minimum contribution requirement would be ‘economically unsound’ and would lead to competitive distortions in the market.” Pitney Bowes Comments at 10; Pitney Bowes Reply Comments at 6.

b. Commission Analysis

The Commission explained that any attempt to account for uniquely and disproportionately associated costs that are attributable by adjusting the Commission’s formula would essentially double-count them (in their entirety or by some lesser amount), in a way that is unnecessary, economically unsound, and would be harmful to the Postal Service and its Competitive product business. Order No. 6043 at 75, 78-79. Pitney Bowes and ASL agree the Commission correctly concluded that double-counting attributable costs through their inclusion in the appropriate share determination would be an “economically unsound” approach that would distort competition.¹⁰⁹ In addition, the Postal Service, ASL, Dr. Panzar, and Pitney Bowes agree that UPS’s suggested

¹⁰⁹ ASL Comments at 29; ASL Reply Comments at 14; Pitney Bowes Comments at 10; Pitney Bowes Reply Comments at 6.

use of attributable cost percentage is tantamount to, or based on, fully distributed costing, which would result in the arbitrary allocation of costs.¹¹⁰ Regardless whether the Commission includes all of Competitive products' attributable costs or some lesser amount of those costs as part of its dynamic formula-based approach (which would result in some amount of double-counting) or uses Competitive products' percentage of the Postal Service's total attributable costs as an estimate of the percentage of institutional costs Competitive products should cover, the result would still be the unnecessary, economically unsound and harmful inclusion of costs. See Order No. 6043 at 75, 78-79.

Failing to rebut this assessment, instead UPS suggests that the Commission could "consider" attributable costs without double-counting them, by using the percentage of costs attributed to Competitive products *compared to* Market Dominant products as a reasonable estimate of the percentage of institutional costs that likewise should be covered by Competitive products. UPS Comments at 47. Again, UPS uses the word "consider" as a proxy for "include" and insists the Commission use Competitive products' percentage of the Postal Service's total attributable costs and require that Competitive products account for the same percentage of the Postal Service's total institutional costs. However, attributable costs and institutional costs move independently from each other. See Figure VIII-2, *infra*. UPS attempts to create an association between two types of costs that are not comparable and then use that fabricated association to include additional costs as part of the appropriate share. However, the relationship between attributable costs and institutional costs, which UPS suggests can be used to allocate institutional costs to Competitive products, does not actually exist. Thus, after considering UPS' arguments, and "the degree to which any costs are uniquely or disproportionately associated with any competitive products"

¹¹⁰ Postal Service Reply Comments at 54; ASL Reply Comments at 21; Panzar Reply Decl. at 6; Pitney Bowes Reply Comments at 11. See *also* Order No. 4402 at 81; Order No. 4963 at 36.

pursuant to 39 U.S.C. § 3633(b), the Commission declines to make any further adjustments to the appropriate share.

5. The Commission Considered the Existence of Uniquely or Disproportionately Associated Costs within Institutional Costs

a. Comments

UPS contends that the Commission failed to follow the court's mandate that it *must* consider all costs uniquely or disproportionately associated with Competitive products. UPS Comments at 1. UPS states that "despite now recognizing that institutional costs uniquely or disproportionately associated with competitive products can exist, the Commission does not identify even *a single dollar* classified as institutional that is uniquely or disproportionately associated with competitive products." *Id.* at 11 (emphasis in original).

In contrast, ASL asserts that the Commission "fully explained" uniquely and disproportionately associated costs and that it "adequately considered all costs that the Postal Service accrues in the course of its business." ASL Comments at 28. Similarly, Pitney Bowes states that the Commission "thoroughly consider[ed] all costs, including the costs identified by UPS, and correctly [held] that there are no costs 'uniquely or disproportionately associated with' competitive products that have not already been addressed under the Commission's existing cost attribution methodology." Pitney Bowes Comments at 4 (footnote omitted); Pitney Bowes Reply Comments at 4. The Postal Service states that the Commission has adequately remedied the deficiencies identified by the court and maintains that the Commission addressed the issues as framed by the court in "the only rational way." Postal Service Comments at 16, 20, see *id.* at 30-31; see *also* Postal Service Reply Comments at 33-36.

Both ASL and Pitney Bowes address UPS's argument that the Commission did not "consider" costs uniquely or disproportionately associated with Competitive products

because no such costs were identified. ASL Reply Comments at 15; Pitney Bowes Reply Comments at 4. ASL observes that, despite UPS's arguments to the contrary, the PAEA and the court do not require the Commission to identify costs that would meet the "uniquely or disproportionately associated" phrase appearing in 39 U.S.C. § 3633(b) if no such costs exist. ASL Reply Comments at 15. ASL explains that "it simply does not follow that the Commission has failed to consider such costs if it has considered the matter and found that none exist." *Id.* (footnote omitted). Pitney Bowes maintains that the Commission "thoroughly considered all costs that the Postal Service accrues, including specific costs identified by UPS" and held that none existed that had not already been accounted for under the current costing methodology. Pitney Bowes Reply Comments at 5 (footnote omitted). It elaborates that, despite UPS's suggestion, *UPS II* and the PAEA "leave open the possibility that the Commission may consider, but not find any such costs." *Id.* The Postal Service observes that, despite UPS's claim otherwise, the Commission has already identified "hundreds of millions of dollars" of institutional costs that would have met the "uniquely or disproportionately associated" phrase appearing in 39 U.S.C. § 3633(b) prior to the significant expansion of cost attribution in Final Order No. 3506. Postal Service Reply Comments at 38 (citing Order No. 6043 at 79-80; Postal Service Comments at 20-21).

b. Commission Analysis

UPS's claim that the Commission has recognized that institutional costs uniquely or disproportionately associated with competitive products can exist, yet fails to identify any that currently exist is misleading. UPS paraphrases the Commission's extensive analysis of the difference between the definition of costs attributable to Competitive products and the definition of costs uniquely or disproportionately associated with Competitive products by stating that the Commission recognized that uniquely or disproportionately associated costs "can exist" within the Postal Service's institutional costs. UPS Comments at 11. UPS then reinterprets "can exist" as meaning that the

Commission found that such costs “may currently exist” in institutional costs. See *id.* at 11. UPS uses this incorrect interpretation to support its position that there are, or at least may be, costs currently classified as institutional costs that are uniquely or disproportionately associated with competitive products and that the Commission has failed to consider them. The Commission addresses UPS’s incomplete and misleading statement as follows.

As the Commission noted in Order No. 6043, cost attribution remained relatively unchanged until the adoption of the incremental cost test in Final Order No. 3506, which allowed the Commission to significantly expand cost attribution and reduce institutional costs. See Order No. 6043 at 27-35. However, UPS’s statement implies that because the Commission acknowledged that at one point there were costs uniquely or disproportionately associated with Competitive products that were classified as institutional costs, it automatically leads to a conclusion that there continue to be the same kinds of costs classified as institutional costs now. That implication, however, is inaccurate. As the Commission explained in Order No. 6043, if the Commission had not made the decision to reclassify these costs as attributable, then under the interpretation of “uniquely or disproportionately associated” costs that the Commission articulated in Order No. 6043 these costs would be relevant to the Commission’s appropriate share determination. *Id.* at 79-80. However, after the issuance of Final Order No. 3506, product-level inframarginal, group-specific, and group-level inframarginal costs calculated as part of Competitive products’ incremental costs *were reclassified as attributable costs*. *Id.* at 29-30. As a result, there are no costs uniquely or disproportionately associated with Competitive products within the Postal Service’s institutional costs. See Section IV.F.2., *supra*.

ASL and Pitney Bowes agree that neither the PAEA nor the court’s remand opinion require the Commission to identify any costs as uniquely or disproportionately associated with Competitive products if none exist. See ASL Reply Comments at 14;

Pitney Bowes Reply Comments at 5. As noted previously, ASL concluded that “it simply does not follow that the Commission has failed to consider such costs if it has considered the matter and found that none exist.” ASL Reply Comments at 15 (footnote omitted). Pitney Bowes concluded that, despite UPS’s suggestion, *UPS II* and the PAEA “leave open the possibility that the Commission may consider, but not find any such costs.” Pitney Bowes Reply Comments at 5.

6. The Commission Considered Whether to Incorporate Unattributed
Inframarginal Costs into the Minimum Contribution Requirement

a. Comments

UPS claims that the Commission failed to apply the court’s “more expansive test” of a meaningful relationship between Competitive products and unattributed inframarginal costs. UPS Comments at 14.

The Postal Service explains that from a logical perspective, proper incremental costing already attributes any costs that are meaningfully related to Competitive products. Postal Service Comments at 25-27. The Postal Service elaborates that this occurs because, under incremental costing, all the costs that would be eliminated if Competitive products were no longer offered are, in fact, attributed to Competitive products. *Id.* at 26-27. Thus, the Postal Service reasons that “a ‘meaningful’ relationship would require a showing that [the] costs alleged to be ‘uniquely or disproportionately associated’ with Competitive products would not be incurred if Competitive products were discontinued.” *Id.* at 27. It elaborates that, consistent with Order No. 6043, “if such a showing could be made, the costs in question[] would be incremental to Competitive products, would be attributed to Competitive products, and would therefore not be classified as institutional.” *Id.* (footnote omitted). The Postal Service agrees with the Commission’s conclusion that a “partial relationship between institutional costs and Competitive products is neither meaningful nor relevant to the

Commission's determination of the appropriate share, and that attempting to allocate such costs in the review of the [appropriate share] requirement would lack justification from an economic, cost-accounting, and policy perspective, as the allocation of costs would be arbitrary, and harmful." *Id.* at 25.

b. Commission Analysis

Unattributed inframarginal costs are variable costs that are caused by the simultaneous handling of both Market Dominant and Competitive products. Order No. 6043 at 81, n.129, 83. Because these costs are jointly incurred, they are not separable into categories where some costs can be shown to have a meaningful relationship with Competitive products and some costs can be shown to have a meaningful relationship with Market Dominant products. See *id.* at 83. UPS asserts that the Commission's finding that unattributed inframarginal costs cannot be untangled and separated into those related to Competitive products and those related to Market Dominant products means it did not apply the court's "more expansive," meaningfully related test. UPS Comments at 56-57. However, the Commission reiterates that its findings are based on an economic reality that these costs specifically do not have a meaningful relationship with products, it is their *very* nature that such a relationship does not exist. See Order No. 6043 at 81-85. Because sound economics dictates that unattributed inframarginal costs have no meaningful relationship with either Competitive or Market Dominant products, unattributed inframarginal costs are properly and accurately classified as institutional costs. Detailed analysis supports the Commission's conclusion that it cannot reasonably estimate which portion of unattributed inframarginal costs are more related to Competitive products than Market Dominant products as estimation implies even a minimal level of accuracy and would be arbitrary. See *id.* at 80-95. UPS fails to meaningfully rebut these findings. Instead, UPS echoes its prior arguments in this proceeding and on appeal that the Commission must randomly assign such costs based on any number of arbitrary links (like the types of approaches that UPS proposes), to be

responsive to the issues identified by the court. See, e.g., UPS Comments at 43-44, 48, 56-57; UPS Brief at 35. In other words, without any supporting or persuasive evidence, UPS claims that a meaningful relationship between unattributed inframarginal costs and products simply exists. For the Commission to adopt such a position, however, would constitute arbitrary and capricious decision-making.

The court directed the Commission to address the following questions on remand concerning unattributed inframarginal costs:

Are some of the Postal Service's institutional costs – and especially its unattributed inframarginal costs – still related in some meaningful way to competitive products, even if those costs cannot be attributed under § 3633(a)(2)? And if so – if, for instance, some of those institutional costs are 'uniquely or disproportionately associated with competitive products,' 39 U.S.C. § 3633(b) – might they need to be accounted for when the Commission issues regulations under another provision of the Accountability Act?

UPS II, 955 F.3d at 1045. The court never indicated that the Commission must find a meaningful relationship if none exists. Moreover, even if the Commission found a meaningful relationship exists (which it does not), the court did not instruct the Commission to incorporate those unattributed inframarginal costs into the appropriate share. Instead, the court correctly recognized “that the Commission might decide against revising its bottom-line judgment [to readopt a dynamic formula-based approach to calculating the appropriate share], given the other factors the Commission must consider under § 3633(b) and the latitude that the text affords the Commission in making a final determination.” *Id.* at 1051. Applying the court's instruction in the manner UPS suggests would contravene the text and purpose of the PAEA and the decision rendered in *UPS II*.

Further, even if the court had implied the Commission must engage in such an exercise (which it did not), any assignment of unattributed inframarginal costs to Competitive products would be arbitrary and economically unsound because the

relationship between cost and product would not be meaningful. Instead, the relationship would be artificial. The Commission illustrated this concept as part of Order No. 6043, when it provided examples of how the distribution of institutional costs based on relative shares of volumes and attributable costs can distort accurate costing. See Order No. 6043 at 87-90.

7. The Commission's Use of Sound Economic Measurement is Reasonable

a. Comments

UPS contends that the Commission's use of "economically sound" measurement "employs a double standard" because other methodologies employed by the Commission rely on estimates, judgments, and assumptions. UPS Comments at 14-15. UPS contends that being unable to "precisely identify which institutional costs are uniquely or disproportionately associated with competitive products is not sufficient for the Commission to abdicate its responsibility to consider them." *Id.* at 11. UPS insists that the Commission should try to quantify which institutional costs may be uniquely or disproportionately associated with competitive products "the best it can," "[e]ven if the analysis is difficult or imperfect." *Id.* at 11-12. UPS states that the Commission "fails to identify *any* approach that it has actually tried to use to identify or estimate" institutional costs that are uniquely or disproportionately associated with Competitive products. *Id.* at 12. UPS asserts that the inability to precisely identify cost uniquely or disproportionately associated with Competitive products is insufficient for the Commission to "abdicate" its responsibility to consider those costs. *Id.* at 14.

However, Dr. Panzar counters that the Commission's explanation that the relationship between a cost and the provision of Competitive products must be "discernable and measurable in a manner that is economically sound" is "intuitively sensible and necessary" to "avoid arbitrary and potentially distortive assignments of

costs that bear no economically meaningful relationship with a specific product or group of products.” Panzar Decl. at 27.

Similarly, ASL posits that the Commission was correct when it concluded that the “relationships between a cost and a product, or group of products ‘must be discernable and measurable in a manner that is economically sound’ to be considered meaningful” and that no such costs are identifiable within institutional costs. ASL Comments at 29-30. ASL agrees with the Commission’s rejection of the premise that the phrase “uniquely or disproportionately associated” means the economically sound allocation of costs based on something other than cost causality. *Id.* at 22. ASL supports the Commission’s conclusion that “the relationship of costs considered ‘uniquely or disproportionately associated with’ a competitive product or group of products must be ‘discernable and measurable in a manner that is economically sound.’” ASL Reply Comments at 18 (quoting Order No. 6043 at 54). ASL explains that “[e]ven if the association can be something less than [a reliably identified causal relationship], there must be some economically rational relationship; otherwise, the exercise becomes either wholly indeterminate or an excuse to try and smuggle in concepts of fully distributed costing.” ASL Reply Comments at 17.

ASL and Pitney Bowes respond to both UPS’s mischaracterization of equating economically sound or economically meaningful relationships with perfection and UPS’s suggestion that the Commission, despite the absence of economically sound methodologies, should do the best it can to apportion institutional costs to Competitive products. *Id.* (citing UPS Comments at 11-12); Pitney Bowes Reply Comments at 7. First, ASL describes that the inability to reasonably apportion common costs between products based on economically meaningful relationships “is a function of the economic reality, not a question of trying harder or doing better.” ASL Reply Comments at 17. Similarly, Pitney Bowes points out that “[i]t is not a matter of looking harder or having a larger microscope” because for multi-product firms like the Postal Service “there will

necessarily be common costs that cannot reasonably be apportioned between products based on an economically meaningful relationship.” Pitney Bowes Reply Comments at 7. Second, ASL observes that although some imperfect methods for cost allocation may be permissible, they “must be grounded in facts, experience and/or logical relationships” and not inherently arbitrary. ASL Reply Comments at 17-18. ASL elaborates that the approaches favored by UPS are not merely imperfect, they are “arbitrary, results-based approaches to impose artificially high price floors on Competitive products that would allow it to obtain unwarranted benefits at the expense of the Postal Service, mailers, shippers, and end consumers.” *Id.* at 18. Similarly, Pitney Bowes summarizes this UPS argument as criticizing the Commission for not using “more robust ‘imperfect estimations.’” Pitney Bowes Reply Comments at 7 (quoting UPS Comments at 14).

The Postal Service observes that “technical complications preclude rational efforts to further segregate inframarginal costs between Competitive and Market Dominant products” and supports the Commission’s analysis regarding unattributed inframarginal costs in Order No. 6043. Postal Service Comments at 28. The Postal Service notes that the allocation of these costs “runs into an insurmountable threshold barrier,” *i.e.*, that no methodology exists that would permit the Commission to consistently determine which portion of institutional costs are fixed and which are variable (unattributed) inframarginal costs. *Id.* at 28-29.

b. Commission Analysis

As explained in Section IV.F.2., *supra*, the Commission does not impermissibly employ a double standard as UPS contends. Instead, the Commission uses the correct legal standards for different types of proceedings. UPS argues the Commission must try harder to identify meaningful relationships between institutional costs and Competitive products. See UPS Comments at 11-13. UPS claims that a meaningful relationship between some institutional costs and the provision of Competitive products

exists, but because that relationship evades the measurement of economists and cost accountants, the Commission must manufacture one. See *id.* at 11-16. The Commission rejects the urging of UPS to apply the requirement to consider "*the degree to which* any costs are uniquely or disproportionately associated with any competitive products" phrase appearing in 39 U.S.C. § 3633(b) (emphasis added) to mean that the Commission must adopt a rule divorced from all economic meaning. Selecting among the types of approaches offered by UPS would randomly assign costs based on any number of arbitrary connections. Doing so would be inconsistent with the statute, unresponsive to the issues identified by the court, and irrational. The relationship between a cost and the provision of Competitive products must be at a level that is discernable and measurable in a manner that is economically sound to be a relevant consideration of "the degree to which any costs are uniquely or disproportionately associated with any competitive products" phrase appearing in 39 U.S.C. § 3633(b)—as the court summarizes it—"meaningful" (*UPS II*, 955 F.3d at 1045) to the Commission's evaluation of the appropriate share. See Order No. 6043 at 53-54, see also *id.* at 73, 81, 83-84, 92, 95-97. Basing the Commission's consideration on economically sound approaches to setting the appropriate share is a reasonable judgment that is consistent with the text and purpose of the PAEA and the development of postal costing. See Section IV.F.2., *supra*; Order No. 6043 at 11-40.

As the Commission noted previously, institutional costs consist of fixed costs and unattributed inframarginal costs, and only unattributed inframarginal costs are related to the simultaneous handling of both Competitive products and Market Dominant products. The Commission's discussion related to the inability to accurately identify certain institutional costs as costs uniquely or disproportionately associated with Competitive products was in relation to unattributed inframarginal costs, which, due to their nature, cannot be separated in accordance with sound economic principles. See Section V.A.6.b., *supra*; Order No. 6043 at 80-95. UPS insists that the Commission should try to quantify which institutional costs may be uniquely or disproportionately associated

with competitive products “the best it can,” “[e]ven if the analysis is difficult or imperfect.” UPS Comments at 11-12. However, the Commission agrees with Pitney Bowes that, when it comes to these costs, “[I]t is not a matter of looking harder or having a larger microscope.” Pitney Bowes Reply Comments at 7. As reiterated above, the Commission’s findings are based on an economic reality that these costs do not have a meaningful relationship with either Competitive products or Market Dominant products because the relationship between costs and products is inseparable. As a result, the relationship between a cost and the provision of Competitive products is not at a level that is discernable and measurable in a manner that is economically sound.

UPS claims that “the Postal Service treats any cost that cannot be tied to competitive products in an economically perfect manner as though the cost does not exist.” UPS Comments at 16. However, the Postal Service does not ignore institutional costs. In the most recent year for which data are available (FY 2021), Competitive products covered approximately 39.2 percent of total institutional costs (\$13.193 billion out of a total of \$33.634 billion), which represented a 17.95 percent increase over Competitive product contribution the year before. FY 2021 ACD at 96. This contribution dwarfs the volume share of Competitive products (5.97 percent of total mail volume in FY 2021). FY 2021 Financial Report, App’x A). Thus, the best available evidence contradicts UPS’s claim.

8. The Commission Rejects the Arbitrary Allocation of Institutional Costs to Market Dominant versus Competitive Products as Unreasonable

a. Comments

UPS states that the Commission’s conclusion that the allocation of Market Dominant and Competitive products’ costs would be arbitrary due to their simultaneous handling “says nothing about whether some costs are uniquely or disproportionately associated with competitive products.” UPS Comments at 56. UPS also argues that

the Commission erred in concluding that it could not reasonably separate a cost component's institutional costs into unattributed inframarginal costs and fixed costs categories and then further segregate the unattributed inframarginal costs into those that are meaningfully related to the provision of Competitive products. *Id.*; Order No. 6043, at 84. UPS claims that the separation of these costs to measure uniquely or disproportionately associated costs is not needed and that “[t]he best solution is to measure stand-alone market-dominant costs first, so the Commission will have a realistic estimate of the scope of costs uniquely and disproportionately associated with competitive products.” UPS Comments at 56-57. UPS asserts that the Commission does not directly address stand-alone costs, make any attempt to model them, and categorically rejects any attempt to look beyond short-run incremental costs. *Id.*

ASL asserts that “the notion that the minimum contribution requirement can be used to ‘plus up’ or hedge alleged imprecision in the cost attribution methodology is not only economically unsound but raises other concerns as well,” such as inefficient pricing. ASL Comments at 22. It further asserts that cost attribution models should only be improved through the “established, transparent process for refining cost model,” and not through the appropriate share requirement. *Id.* at 22-23.

ASL agrees with the Commission’s finding that employing arbitrary methods of cost allocation as it relates to institutional costs would seriously undermine the Postal Service’s ability to compete and degrade the integrity of the Commission’s regulatory costing methodology. *Id.* at 30. Similarly, Pitney Bowes agrees with the Commission that the arbitrary assignment of some quantity of institutional costs to competitive products would be “economically unsound,” “degrade the integrity of regulatory costing models,” and distort competition. Pitney Bowes Comments at 4. Both ASL and Pitney Bowes note that the arbitrary assignment of costs would result in price increases and market distortions that would harm mailers, shippers, and consumers. *Id.*; ASL Comments at 3. Finally, the Postal Service concurs with the Commission’s analysis

that, assigning an arbitrary share of institutional costs to Competitive products is both a form of fully distributed costs and could cause harm. Postal Service Comments at 29-30.

b. Commission Analysis

Throughout this docket and on appeal, UPS reiterates its argument that by refusing to separate institutional costs in an arbitrary manner, the Commission ignores the requirement to consider "the degree to which any costs are uniquely or disproportionately associated with any competitive products" appearing in 39 U.S.C. § 3633(b). See, e.g., UPS Comments at 1, 9-29; UPS Reply Comments at 1; UPS Brief at 3, 17-18. However, UPS fails to rebut the Commission's conclusion that nothing in the PAEA requires such action and that doing so would contravene the intent of the PAEA as well as constitute arbitrary and capricious agency action.

Several commenters agree with the Commission's assessment regarding the arbitrary assignment of institutional costs. ASL, Pitney Bowes, and the Postal Service all agree that employing arbitrary methods of cost allocation as it relates to institutional costs would undermine the Postal Service's ability to compete, degrade the integrity of the Commission's regulatory costing methodology, would be economically unsound, and could harm the Postal Service and consumers.¹¹¹

Arbitrary cost allocation is "bereft of any economic meaning." Order No. 6043 at 86 (citing 2020 Panzar Paper at 9). Depending on the approach used to make the arbitrary allocation, it can create vastly differing impressions regarding the financial viability of products. Order No. 6043 at 90. Without proper costing data, "[a] firm

¹¹¹ ASL Comments 3, 30; Pitney Bowes Comments at 4; Postal Service Comments at 29-30.

cannot set appropriate prices or rates and may make pricing and production decisions which lead to reduced profits or even losses.”¹¹²

Most significantly of all, the arbitrary allocation of institutional costs to Competitive products could undermine the Postal Service’s ability to effectively compete in the market for competitive postal services because it could force the Postal Service to either stop offering products that were actually helping to cover institutional costs, or to raise product prices to unsustainable levels relative to other competitors in the market.¹¹³ Either outcome would lead to less rigorous competition in the market. Order No. 6043 at 91. Customers would have fewer options and there would be fewer constraints on the prices charged by competitors. *Id.* Furthermore, if the Postal Service were to have to stop offering a product deemed “unprofitable” despite covering its incremental costs, that product’s allocation or assigned portion of institutional costs would then be forced upon the remaining Competitive products, and, eventually, Market Dominant products. *Id.*

It is for this reason that experts in postal economics and cost accounting have concluded that, generally speaking, “[a]bove [attributable costs], a regulated firm like the Postal Service should be allowed to set markups that, in the judgment of Postal Service management, are responsive to the sensitivity of demands for the services and

¹¹² Order No. 6043 at 90 (citing Michael D. Bradley et al., *Measuring Product Costs For Ratemaking: The United States Postal Service*, in Regulation and the Nature of Postal and Delivery Services, ed., M. A. Crew and P. R. Kleindorfer (Boston: Kluwer Academic Publishers, 1993) (1993 Bradley et al. Paper), at 133).

¹¹³ See Order No. 6043 at 91. See also ASL Comments at 22 (“The notion that the minimum contribution requirement can be used to ‘plus up’ or hedge alleged imprecision in the cost attribution methodology . . . [would] prevent[] the Postal Service from pricing near incremental cost where necessary to compete, as profit-maximizing entities do.”); Public Representative Reply Comments at 6 (“The Postal Service’s competitive products exist in a market for differentiated package delivery. As such, the profit-maximizing markup for these products will be lower than that for market-dominant products, over which the Postal Service exercises market power. If the Postal Service’s markups are too high, they will lose volume, and therefore contribution, to rivals such as UPS.”) (footnote omitted).

sensitive to competitors' reactions."¹¹⁴ One of the theoretical underpinnings of the PAEA's regulatory scheme is that allowing the Postal Service to exercise its pricing discretion to recover institutional costs by pricing to the market (*i.e.*, based on demand sensitivities and competitors' reactions) allows for the greatest possible contribution that can be obtained given existing market conditions. See Panzar Decl. at 5. Even if such profit-maximizing prices are insufficient to recover all institutional costs, in theory the total recovery under those prices should still be greater than it would be if institutional costs were arbitrarily allocated into product price floors. See *id.* If the Postal Service's downward pricing flexibility were to be seriously curtailed as a result of the arbitrary allocation of institutional costs, then the Postal Service could find itself unable to reduce prices for Competitive products even when doing so is necessary to compete in the market for competitive postal services.¹¹⁵ If this were to occur, it would result in fewer units sold, and hence less overall contribution to institutional costs than if the Postal Service had been permitted to recover the institutional costs by pricing to the market. See Panzar Decl. at 5. UPS's interpretation of the appropriate share requirement's

¹¹⁴ *Id.* at 86 (citing 2020 Panzar Paper at 23). As Panzar further explains, incremental costs (which currently form the basis for attributable costs) are "uniquely important as a guide in determining the specific rates which will provide the maximum contribution to the overhead [institutional cost] burden and thus to net income." Panzar Decl. at 21-22 (quoting William Baumol et al.; *The Role of Cost in the Minimum Pricing of Railroad Services*, *Journal of Business*, Vol. 35, No. 4, 357, 362 (Oct. 1962).). In fact, incremental costs form "the *only* relevant cost data relevant for determining efficient price floors" Panzar Decl. at 21 (emphasis in original). This is because "[a]s a general rule, any rate below incremental costs is both unprofitable and socially wasteful of resources because the additional (incremental) revenue obtained is less than the additional cost incurred." *Id.* at 21 (quoting William Baumol et al.; *The Role of Cost in the Minimum Pricing of Railroad Services*, *Journal of Business*, Vol. 35, No. 4, 357, 362 (Oct. 1962).). "Thus, while incremental costs should not determine prices or rates, they set the lower boundary (and demand conditions and regulation the upper boundary) within which pricing decisions should be made." Panzar Decl. at 22 (emphasis omitted) (quoting William Baumol et al.; *The Role of Cost in the Minimum Pricing of Railroad Services*, *Journal of Business*, Vol. 35, No. 4, 357, 362 (Oct. 1962).). However, "[t]he margin above incremental costs that maximizes the contribution depends upon the price sensitivity of demand, determined primarily by the alternatives available to shippers." Panzar Decl. at 22 (quoting William Baumol et al.; *The Role of Cost in the Minimum Pricing of Railroad Services*, *Journal of Business*, Vol. 35, No. 4, 357, 362 (Oct. 1962).).

¹¹⁵ See *id.* See also ASL Comments at 22 ("[P]ricing near incremental cost[s] where necessary to compete[] [is what] profit-maximizing entities do.").

purpose would inherently have the effect of extending cost allocation based on extended inferences of causation in a manner akin to fully distributed costing, and therefore reducing the size of the residual over which the Postal Service exercises its pricing discretion, which would limit the Postal Service's ability to set profit-maximizing markups that maximize contribution to institutional costs.

As summarized above, applying the requirement of 39 U.S.C. § 3633(b) to consider "the degree to which any costs are uniquely or disproportionately associated with any competitive products" as UPS urges would be unreasonable and contravene intent of the PAEA. By contrast, the Commission's approach is consistent with the evolution of postal costing, which has always relied on economic and cost accounting principles, consistent with the intent of the PAEA. See Order No. 6043 at 11-40.

With respect to UPS's claim that the Commission has non-arbitrary options using stand-alone Market Dominant costs, it asserts that the difference between the actual total costs of the Postal Service and the modeled stand-alone costs of Market Dominant products would be uniquely or disproportionately associated with Competitive products. See UPS Comments at 56-57. UPS explains that modeling the stand-alone costs of a product (or group of products) is a way of estimating the incremental costs of the product (or group of products) and can form the basis for a test of reasonableness of the rates for the product (or group of products). See *id.* at 50-51. But as UPS acknowledges, a customer typically uses stand-alone costs to challenge "a rate that it regards as excessive" (*id.* at 51), and not to challenge rates for being too low. Moreover, UPS acknowledges that what it seeks from a stand-alone cost test is to "reveal which aspects of the Postal Service's operations are the result of competitive products." *Id.*

The stand-alone costs of Market Dominant products might be relevant to a hypothetical question of whether the rates for Market Dominant products are excessive; however, the PAEA addresses that possibility via the price cap on Market Dominant rates rather than through a stand-alone costing exercise. *Compare* 39 U.S.C. § 3622 *with id.* § 3633. To the extent that the difference between actual total costs and the stand-alone costs of Market Dominant products would reflect the cost of adding (or removing) Competitive products, it would be a more convoluted and error-prone method of estimating the incremental cost of Competitive products than the method already employed by the Commission. See Section VIII.C.3., *infra*. As commenters note, UPS seeks to model a hypothetical efficient stand-alone Market Dominant enterprise as a means of ensuring that any existing inefficiencies in the Postal Service are imputed exclusively to Competitive products. See, e.g., Pitney Bowes Reply Comments at 14. As detailed in Section VIII.C.3., *infra.*, such an approach is unreasonable.

B. The Prevailing Competitive Conditions in the Market and Other Relevant Circumstances

1. Background

In addition to considering “the degree to which any costs are uniquely or disproportionately associated with any competitive products,” each time it reviews the appropriate share, the Commission must consider “all relevant circumstances, including the prevailing competitive conditions in the market” 39 U.S.C. § 3633(b). In Order No. 6043 and prior orders in this docket, the Commission explained how the dynamic formula-based approach to calculating the appropriate share is designed to capture these considerations.¹¹⁶ The Commission also assessed the prevailing competitive conditions in the market for competitive postal services and how the formula-based

¹¹⁶ Order No. 6043 at 97-105; Order No. 4963 at 19-29; Order No. 4742 at 47-57; Order No. 4402 at 11-53.

approach would have performed had it been in effect since it was initially promulgated in 2019. Order No. 6043 at 105-09; Order No. 4963 at 4-12.

a. The Dynamic Formula-Based Approach

Prior to Docket No. RM2017-1, in which the Commission conducted its second required 5-year review of the appropriate share requirement, the appropriate share was set at a static 5.5 percent of institutional costs. However, in Docket No. RM2017-1, the Commission noted significant developments that had occurred in the market for competitive postal services since the appropriate share was initially set, including surging demand, the development of “co-opetition” between competitors in the market, steady increases in revenue and profit for all competitors, and growth in the Postal Service’s market share and Competitive product volume. Order No. 4963 at 4-12, 20; Order No. 4402 at 12. Order No. 4963 provided an in-depth discussion of the development of the market for competitive postal services since the PAEA was enacted in 2007, describing changes in market size, demand, market share, revenue, and pricing for the main competitors in the market. Order No. 4963 at 4-12. Order No. 6043 updated this analysis to consider further changes occurring in the market after issuing Order No. 4963, including changes following the outbreak of the COVID-19 pandemic in FY 2020. Order No. 6043 at 105-09.

Although the Commission concluded that the market for competitive postal services remained healthy and competitive, the Commission found it appropriate to implement a dynamic approach to setting the appropriate share that would be more responsive to changing market conditions and would more transparently tie the appropriate share to the prevailing competitive conditions in the market and other relevant circumstances. Order No. 6043 at 98; Order No. 4963 at 19-20, 29; Order No. 4402 at 12. The Commission historically considered qualitative considerations when evaluating these factors. Order No. 6043 at 98-99. Order No. 4963 at 20; Order No. 4402 at 8-11. The Commission found that most of these qualitative considerations

would be implicitly captured by evaluating the Postal Service's market power in the market for competitive postal services. Order No. 6043 at 99; Order No. 4963 at 20; Order No. 4742 at 49-52, 55-57.

Market power is a firm's ability to price a product or service higher than the cost of producing it. Order No. 6043 at 99; Order No. 4963 at 20. Generally, the higher a firm can price its products above costs, the more market power the firm possesses. Order No. 6043 at 99; Order No. 4963 at 20. However, a firm's market power is constrained both by the elasticity of demand for its products (*i.e.*, the highest price its customers are willing to pay), and by the firm's market share and the conduct and performance of other competitors competing in the market. Order No. 6043 at 99; Order No. 4963 at 2021. As a result, market power as a concept embodies both absolute and relative aspects: a firm's absolute market power is its ability to raise prices with respect to its own customers and its relative market power (*i.e.*, its market position), is its capacity to exercise market power relative to its competitors. Order No. 6043 at 99; Order No. 4963 at 21.

The Postal Service's absolute market power and market position determine the capacity of Competitive products collectively to generate profit that can be contributed to institutional costs. Order No. 6043 at 99; Order No. 4963 at 21-22. The formula-based approach is designed to determine the year-over-year change in this capacity and adjust the appropriate share upwards or downwards accordingly. Order No. 6043 at 99; Order No. 4963 at 22. This approach implicitly captures the competitive conditions in the market for competitive postal services because those conditions are reflected in the Postal Service's market power and market position. Order No. 6043 at 99; Order No. 4963 at 29.

The formula is made up of two components: the CCM and the Competitive Growth Differential (CGD). The CCM measures the Postal Service's absolute market power with respect to its Competitive products. Order No. 6043 at 99; Order No. 4963 at 22-24. The CGD measures the change in the Postal Service's market position in the market for competitive postal services from year-to-year. Order No. 6043 at 99-100; Order No. 4963 at 25-26.

The CCM is a modified form of a traditional Lerner index, which measures the difference between the marginal cost of producing a product and the amount of revenue a firm can realize from that product. Order No. 6043 at 100; Order No. 4963 at 23; Order No. 4402 at 17. The CCM is calculated as follows:

$$\text{Competitive Contribution Margin} = \frac{\text{Total Revenue} - \text{Total Attributable Cost}}{\text{Total Revenue}}$$

Order No. 6043 at 100; Order No. 4963 at 23. It assesses the Postal Service's market power with respect to all Competitive products collectively for a given fiscal year based on the difference between the total attributable cost of producing Competitive products collectively and the amount of revenue the Postal Service can realize from Competitive products collectively. Order No. 6043 at 100; Order No. 4963 at 23-24. Through the operation of the formula, this result is then compared to the prior year to assess the year-over-year change. Order No. 6043 at 100; Order No. 4963 at 22-23. Values for the CCM should typically range between 0 and 1, with higher values indicating more market power. Order No. 6043 at 100; Order No. 4963 at 24; Order No. 4402 at 36.

The second formula component, the CGD, is designed to assess the growth or decline of the Postal Service's market position from year-to-year and captures the change in the size of the Postal Service's Competitive business relative to that of its competitors. Order No. 6043 at 100; Order No. 4963 at 25; Order No. 4742 at 23, 27. This is determined by comparing the year-over-year change in the Postal Service's Competitive product revenue to the year-over-year change in the collective revenue of the Postal Service's competitors in the market for competitive postal services.¹¹⁷ This relative growth is then weighted by the Postal Service's market share.¹¹⁸ The CGD is calculated as follows:

Competitive Growth Differential

$$= \text{Market Share}_{USPS} * (\% \Delta \text{Revenue}_{USPS} - \% \Delta \text{Revenue}_{C\&M})$$

Order No. 6043 at 101; Order No. 4963 at 25.

Weighting by the Postal Service's market share reduces the influence of the Postal Service's relative growth on the appropriate share, which reflects the constraints that the Postal Service's competitors and its market share place on its capacity to generate greater contribution from Competitive products. Order No. 6043 at 101; Order No. 4963 at 25; Order No. 4742 at 26-28. As the Postal Service gains market share, the magnitude of this reduction decreases, because the Postal Service faces fewer

¹¹⁷ Order No. 6043 at 100-01; Order No. 4963 at 25; Order No. 4742 at 23. The Commission uses revenue rather than volume to measure the size of the market because there are problems of both availability and comparability associated with the relevant volume data. Order No. 4402 at 23; Order No. 4742 at 24; Order No. 6043 at 101 n.147.

¹¹⁸ Order No. 6043 at 101; Order No. 4963 at 25; Order No. 4742 at 23-24. The Postal Service's market share is calculated as:

$$\text{Market Share}_{USPS} = \frac{\text{Revenue}_{USPS}}{\text{Revenue}_{USPS} + \text{Revenue}_{C\&M}}$$

Id.

constraints on its ability to gain revenue relative to its competitors. Order No. 6043 at 101; Order No. 4963 at 25.

Revenue data for the Postal Service are drawn from the annual Product Finances Analysis that the Commission produces each year based on financial reporting from the Postal Service, while revenue data for the Postal Service's competitors are drawn from United States Census Bureau data specific to the "Couriers and Messengers," or "C&M," subsector of the economy.¹¹⁹ All revenue data are adjusted for inflation.¹²⁰

The full formula, including both the CCM and the CGD, is as follows:

$$AS_{t+1} = AS_t * (1 + \% \Delta CCM_{t-1} + CGD_{t-1})$$

$$\text{If } t = 0 = \text{FY 2007, } AS = 5.5\%$$

Where,

AS = Appropriate Share¹²¹

CCM = Competitive Contribution Margin

CGD = Competitive Growth Differential

t = Fiscal Year

Order No. 6043 at 102; Order No. 4963 at 25.

¹¹⁹ Order No. 6043 at 101; Order No. 4963 at 25-26; Order No. 4402 at 23-27. Prior orders detail these revenue sources. See Order No. 4963 at 25-26; Order No. 4402 at 23-29.

¹²⁰ Order No. 6043 at 101; Order No. 4963 at 25-26; Order No. 4742 at 24-25, 29.

¹²¹ This figure is expressed as a percentage and rounded to one decimal place for simplicity and consistency with the Commission's past practice of expressing an appropriate share using one decimal place. Order No. 6043 at 102 n.150; Order No. 4963 at 26, n.59; Order No. 4742 at 38, n.46.

Under the formula-based approach, the appropriate share is adjusted annually by using the formula to calculate the minimum appropriate share for the upcoming fiscal year, and the updated figure is reported as part of the Commission's ACD.¹²² To calculate an upcoming fiscal year's appropriate share percentage (AS_{t+1}), the formula multiplies one plus the sum of the prior fiscal year's CGD and percentage change in the CCM, $(1 + \% \Delta CCM_{t-1} + CGD_{t-1})$, by the current fiscal year's appropriate share (AS_t).¹²³ Both components of the formula are given equal weight.¹²⁴

The formula is recursive in order to incorporate year-over-year changes in the market for competitive postal services, with the formula's calculation beginning in FY 2007 with an appropriate share value of 5.5 percent.¹²⁵ FY 2007 was the first full fiscal year after the PAEA was enacted, and the 5.5 percent value was based on Competitive products' historic contribution to institutional costs at that time.¹²⁶ Thus, a recursive calculation allows the resulting appropriate share to capture the impact of market fluctuations since the PAEA's enactment up to the present.¹²⁷

In prior orders in this docket, the Commission explained how the formula-based approach captures the majority of the qualitative considerations that the Commission historically relied upon in evaluating the prevailing competitive conditions in the market and other relevant circumstances.¹²⁸ With respect to the prevailing competitive conditions in the market, the Commission has historically considered the existence (or nonexistence) of evidence of the Postal Service having a competitive advantage in the

¹²² Order No. 6043 at 102; Order No. 4963 at 27; Order No. 4742 at 38-39. For an example of how the formula functions from year-to-year, see Order No. 4742 at 39-40.

¹²³ Order No. 6043 at 102; Order No. 4963 at 27; Order No. 4742 at 39.

¹²⁴ Order No. 6043 at 102; Order No. 4963 at 27; Order No. 4742 at 43-46.

¹²⁵ Order No. 6043 at 103; Order No. 4963 at 27; Order No. 4742 at 40.

¹²⁶ Order No. 6043 at 103; Order No. 4963 at 27; Order No. 4742 at 30-31.

¹²⁷ Order No. 6043 at 103; Order No. 6043 at 103; Order No. 4742 at 40.

¹²⁸ Order No. 6043 at 103; Order No. 4963 at 28-29; Order No. 4742 at 49-52, 55-57.

market for competitive postal services; changes to the Postal Service's market share; and changes to the market for competitive postal services and the Postal Service's competitors.¹²⁹

With respect to competitive advantage, the CCM is a measure of the Postal Service's market power. Order No. 6043 at 103. The higher the CCM, the more market power the Postal Service has, and an increase in the CCM indicates an increase in competitive advantage for Competitive products collectively. Order No. 6043 at 103; Order No. 4742 at 9. The CGD directly incorporates the Postal Service's market share. Order No. 6043 at 103; Order No. 4742 at 51. Finally, both formula components capture changes in the market for competitive postal services and the competitors in it. The changing revenues and market shares of the various competitors in the market, which are inputs to the formula components, reflect market growth or contraction and the entry or exit of competitors. Order No. 6043 at 104; Order No. 4742 at 51-52.

With respect to other relevant circumstances, the Commission has considered changes in Competitive product offerings and the mail mix; uncertainties in the marketplace; and the risks associated with setting the appropriate share either too high or too low.¹³⁰ The formula-based approach captures changes caused by product transfers and changes to the mail mix. Order No. 6043 at 104; Order No. 4742 at 55. The revenue associated with any mail volume shifting from the Market Dominant to the Competitive product category (whether as a result of a product transfer or of changing consumer demand) would be incorporated into both the CCM and the CGD, both of

¹²⁹ Order No. 6043 at 103; Order No. 4402 at 8-9 (citing Order No. 1449 at 13-19).

¹³⁰ Order No. 6043 at 104; Order No. 4963 at 162; Order No. 4402 at 45-46.

which use Competitive product revenue as an input.¹³¹ The formula-based approach also captures uncertainties in the market to the extent that changes in demand or other macroeconomic conditions result in changes in costs, revenue, and/or market share for the various competitors in the market, as these all serve as inputs to both formula components. Order No. 6043 at 104; Order No. 4742 at 56. Similarly, efforts at innovation within the market for competitive postal services and changes in e-commerce would be reflected in the CGD to the extent that they affected the Postal Service and its competitors' respective revenues and market shares. Order No. 6043 at 104; Order No. 4742 at 56. Finally, the formula-based approach accounts for the risks associated with setting the appropriate share too high by limiting increases in the appropriate share to no more than appropriate to account for growth in the Postal Service's market power and market position. Order No. 6043 at 104; Order No. 4742 at 56.

¹³¹ Order No. 6043 at 104; Order No. 4742 at 55. In Order No. 4402, the Commission identified four products that had been transferred from the Market Dominant to the Competitive product list after the Commission's review of the appropriate share requirement in 2012: Single-Piece Parcel Post; Outbound Single-Piece First-Class Mail International Packages (Small Packets) and Rolls; Inbound Surface Parcel Post; and First-Class Mail Parcels. Order No. 4402 at 46. The Commission also noted that the Postal Service's Market Dominant volume was declining, while its Competitive product volume was increasing. *Id.* at 47. The Commission noted, however, that Competitive product volume continued to make up only a small portion of the Postal Service's total mail volume and that the effect of these product transfers and mail mix changes was adequately captured by the formula-based approach. Order No. 4963 at 163-65.

In Order No. 6043, the Commission noted that there had been one additional product transfer to the Competitive product list, consisting of international negotiated service agreements (NSAs). Order No. 6043 at 109 n.165. When Order No. 6043 issued, another potential product transfer related to the Bound Printed Matter Parcels product was pending, but the Commission denied that transfer request. *Compare id. with* Docket No. MC2021-78, Order Denying Request to Transfer Bound Printed Matter Parcels to the Competitive Product List, February 10, 2022 (Order No. 6105).

After Order No. 6043 was issued, 297 Post Office Box locations transferred from the Market Dominant to the Competitive Product List. See Docket No. MC2022-46, Order Approving Request to Transfer Additional Post Office Box Service Locations to the Competitive Product List, July 21, 2022 (Order No. 6234). Although Competitive product volume has continued to increase, it still makes up only a small portion of the Postal Service's total mail volume (5.97 percent in FY 2021). See FY 2021 Financial Report, App'x A. The Commission confirms that the formula-based approach adequately captures the effect of product transfers and mail mix changes.

The Commission continues to find the risks associated with the appropriate share being set too low to be minimal, both because there is no evidence of the Postal Service ever having engaged in anticompetitive behavior and because the Postal Service has strong incentives to maximize profits and little incentive to underprice its Competitive products.¹³² To the extent any such theoretical risk does exist, the Commission finds that the formula-based appropriate share provides a sufficiently high markup on Competitive product prices collectively to prevent any anticompetitive pricing by the Postal Service. Order No. 6043 at 105.

b. The State of Competition in the Market for Competitive Postal Services

The Commission assessed the current state of competition in the market for competitive postal services in Order No. 4963 and Order No. 6043. As the Commission has explained, at the time the appropriate share requirement was initially set, the postal regulatory system was undergoing substantial change because of the enactment of the PAEA and the resultant bifurcation of Market Dominant and Competitive products. Order No. 4963 at 4. In promulgating its initial Competitive product rules in Docket No. RM2007-1, the Commission set the appropriate share at 5.5 percent of total institutional costs. Order No. 4963 at 4; Order No. 43 at 91, 138. In doing so, the Commission considered various proposals for how best to quantify the appropriate share, including “equal unit contribution,” “equal percentage markup,” “markup of competitive products’ attributable costs,” and “percentage of revenues.”¹³³ In setting the appropriate share at 5.5 percent, the Commission selected an “easily understood” percentage of total institutional costs based on Competitive products’ historic contribution to institutional costs during the previous two fiscal years. Order No. 4963 at 5; Order No. 26 ¶¶ 3050,

¹³² See Order No. 4742 at 56-57; Order No. 4963 at 11-12; Order No. 6043 at 104-05.

¹³³ Order No. 4963 at 4-5; See Docket No. RM2007-1, Order Proposing Regulations to Establish a System of Ratemaking, August 15, 2007, ¶ 3050 (Order No. 26).

3059. The Commission was also “mindful of the risks of setting [the appropriate share] too high, particularly at the outset of a new system of regulation.” Order No. 4963 at 5; Order No. 26 ¶ 3058.

Five years later, in Docket No. RM2012-3, the Commission maintained the appropriate share at 5.5 percent of total institutional costs. Order No. 4963 at 5; Order No. 1449 at 26. At that time, the Postal Service had only offered products in the Competitive product category for 5 years. In making its determination, the Commission noted that there had been a lack of significant increase in the Postal Service’s market share between FY 2007 and FY 2011. Order No. 4963 at 5; Order No. 1449 at 16-18. The Commission also noted several market uncertainties that had “the potential to alter the relationship of attributable costs to institutional costs,” and stated that “[t]hese uncertainties could affect the appropriate share contribution requirement in the future.” Order No. 4963 at 5; Order No. 1449 at 23, 24. Without any evidence that the Postal Service was benefiting from an unfair competitive advantage or that the market was not competitive, the Commission determined that maintaining the appropriate share at 5.5 percent was the correct course. Order No. 4963 at 5; Order No. 1449 at 16-19.

In Order No. 4963, issued in January 2019, the Commission found that after its previous review of the appropriate share in Docket No. RM2012-3 a clearer picture of the market for competitive postal services and the Postal Service’s position within that market had emerged. Order No. 4963 at 5. One of the key developments in the market had been growing demand, driven largely by substantial increases in e-commerce sales. *Id.* at 5-6. In Order No. 6043 the Commission noted that this trend had increased significantly because of the COVID-19 pandemic, which began during FY 2020. Order No. 6043 at 105, 107-09.

In Order No. 4963, the Commission explained that the market for competitive postal services consists of three primary competitors that make up most of the market—the Postal Service, Federal Express Corporation (FedEx), and UPS—and one of the

primary ways these three competitors have grown to compete with each other is through firm specialization and product differentiation. Order No. 4963 at 8. Each firm specializes in certain types of delivery—FedEx in international and express delivery, UPS in business-to-business delivery, and the Postal Service in last-mile business-to-consumer delivery of lightweight parcels. *Id.* at 8-9. Each competitor offers products with differences in a range of features, including price, service, reliability, tracking features, and the availability of ancillary services such as insurance and return options. *Id.* at 9.

In addition to firm specialization and product differentiation, the three primary competitors also engage in unique strategies to minimize their costs and lure higher-volume commercial customers. *Id.* Although each competitor offers published prices available to all customers, each also tries to gain business through agreements involving non-published prices, which offer lower, non-published rates, often in exchange for volume commitments. *Id.* This results in a two-tiered pricing structure for the overall market, consisting of published rates for retail customers and lower, non-published rates for higher-volume commercial mailers. *Id.*

Competitors in the market for competitive postal services also cooperate with each other, using each other's specializations to minimize their own delivery costs, a behavior known as "co-opetition." *Id.* The market consists of various components, including an upstream portion that features collection, processing, and transportation functions and a downstream portion that features last-mile delivery. *Id.* at 9-10. Examples of "co-opetition" include, for the upstream portion of the market, the Postal Service contracting with FedEx for FedEx to provide the Postal Service with airport-to-airport transportation of parcels within the United States, and for the downstream portion, UPS and FedEx using the Postal Service to complete last-mile delivery of their parcels. *Id.* at 10. Similarly, the Postal Service also provides last-mile parcel delivery for customers such as ASL, with ASL's own transportation and distribution network

performing the upstream work. *Id.* This “co-opetition” results in lower costs for each of the three major competitors, which in turn lowers the overall cost of delivering parcels and improves the productive efficiency of the market. *Id.*

In Order Nos. 4963 and 6043, the Commission found that the health of the market for competitive postal services could be seen in the major competitors’ prices, which have all steadily increased since the PAEA’s enactment. *Id.* at 10-12; Order No. 6043 at 107-09. All three major competitors have been increasing prices annually as the market has expanded, and cumulative price increases by the respective competitors have tended to converge. Order No. 4963 at 11-12; Order No. 6043 at 107. The Commission also found that the health of the market could be seen in the respective competitors’ revenues, which had all increased steadily since the PAEA’s enactment—especially after the outbreak of the COVID-19 pandemic. Order No. 4963 at 7; Order No. 6043 at 107-08.

In Order No. 6043, the Commission assessed the performance of the formula-based approach since it was initially issued in 2019 and concluded that despite the unforeseeable market growth that had occurred since 2019 due to the COVID-19 pandemic, the formula-based approach had functioned as intended. Order No. 6043 at 105-09. The CCM increased substantially, representing an increase in the Postal Service’s absolute market power due to elevated demand and limited supply in the market for competitive postal services. *Id.* at 106-07. The CGD grew more modestly, illustrating that while the overall size of the market had increased, the Postal Service’s market share had only increased 2.1 percentage points since FY 2019. *Id.* at 107. The Commission found that the market for competitive postal services remained competitive and that the formula-based approach had adequately captured the prevailing competitive conditions in the market and other relevant circumstances. *Id.* at 108-09.

c. Conclusion

In Order No. 6043, the Commission determined that all its conclusions from previous orders in this docket regarding the state of competition in the market for competitive postal services remained valid and that the formula-based approach had functioned as intended despite unforeseeable market growth following the outbreak of the COVID-19 pandemic. *Id.* at 98-109. The Commission thus concluded that the formula-based approach continued to adequately account for the prevailing competitive conditions in the market and other relevant circumstances. *Id.* at 109. Comments received in response to Order No. 6043 generally addressed three topics: the current state of competition in the market for competitive postal services; relevant circumstances that the Commission should consider under 39 U.S.C. § 3633(b) as part of its review of the appropriate share; and comments specific to the formula. The Commission addresses each of these topics below.

2. The Current State of Competition in the Market for Competitive Postal Services Remains Healthy

a. Comments

The Public Representative, ASL, Pitney Bowes, Dr. Panzar, and PSA all maintain that competition in the market for competitive postal services is healthy and competitive.¹³⁴ These commenters assert that Competitive product revenue exceeds Competitive products' attributable costs (see Panzar Decl. at 7), that the Postal Service has consistently increased Competitive product prices in real terms (see *id.* at 9), that Competitive product contribution to institutional costs has risen significantly and far

¹³⁴ PR Reply Comments at 7; ASL Comments at 18-20; ASL Reply Comments at 2; Pitney Bowes Comments at 8-9; Pitney Bowes Reply Comments at 9-11; Panzar Decl. at 7-11; PSA Comments at 2-5.

exceeds the required minimum,¹³⁵ and that increases in Competitive product contribution to institutional costs have outpaced Competitive product volume growth. See Panzar Decl. at 9. They maintain that there is no evidence of anticompetitive behavior by the Postal Service, of subsidization of Competitive products by Market Dominant products, or of any other competitive deficit in the market for competitive postal services.¹³⁶ They assert that the Postal Service's competitors have thrived, as evidenced by their growth and profitability.¹³⁷ They argue that actual contribution from Competitive products to institutional costs is far greater than any alleged "uniquely or disproportionately associated" costs. Panzar Decl. at 8, 28; ASL Comments at 22-23. ASL, Dr. Panzar, and Pitney Bowes note that the Postal Service's total market share remains relatively modest.¹³⁸

UPS argues that market analysis by the Commission and other commenters has been flawed because it has relied on revenue, rather than volume. UPS Reply Comments at 16, 37-38. UPS contends that "[u]sing revenue to compare the respective shares held by UPS and the Postal Service is misleading because the Postal Service has not set prices at sufficient levels to recover its costs" *Id.* at 16, 38. By volume, UPS asserts that the Postal Service delivered more packages than either UPS or FedEx in 2020, which "highlights that, in just a few short years, the Postal Service rapidly grew to overtake UPS and FedEx in the volume of packages delivered to American homes[,] . . . during a period when the Commission set the appropriate share at an artificially low level, and when the Postal Service failed to recover all of its institutional

¹³⁵ ASL Comments at 15; Panzar Decl. at 10; PR Reply Comments at 7; PR Reply Comments at 16; Pitney Bowes Comments at 8; Pitney Bowes Reply Comments at 9.

¹³⁶ ASL Reply Comments at 2; Pitney Bowes Reply Comments at 10; Panzar Decl. at 8-9; PSA et al. Comments at 2-3.

¹³⁷ ASL Comments at 18-19; Pitney Bowes Comments at 8-9; Panzar Decl. at 11.

¹³⁸ ASL Comments at 2, 19; ASL Reply Comments at 11; Panzar Decl. 11; Pitney Bowes Comments at 8.

costs.” UPS Comments at 38; UPS Reply Comments at 16-17. UPS also maintains that the profits earned by it and other private competitors in the market for competitive postal services do not necessarily show that the market is competitive, because these competitors’ “profits are affected by many factors[,] [including] [e]xternal demand trends, efficiency of . . . operations, the supply of labor, and the cost of other inputs” UPS Reply Comments at 17.

b. Commission Analysis

The Commission has previously explained its reasons for measuring the market for competitive postal services by revenue, rather than by volume. Order No. 4963 at 85-87; Order No. 4742 at 19, 22, 29. One of the distinctive features of the market for competitive postal services is “co-opetition” in the form of the Postal Service performing last-mile delivery for its competitors. Order No. 4963 at 9-10. For a package handled by both the Postal Service and one of its competitors, “co-opetition” leverages each shipper’s specialization and thereby lowers delivery costs for each shipper. See *id.* Additionally, there are serious difficulties involved in determining to whom a package handled by multiple shippers should be assigned for purposes of calculating the market’s size by volume. *Id.* at 86.

Furthermore, a more general problem with the use of volume to measure market size is that Competitive products are heterogenous in terms of size, weight, distance transported, and—because of these factors—value to the shipper.¹³⁹ Trends in the e-commerce market (occurring at a heightened extent and speed due to the COVID-19 pandemic) have contributed to volume growth of the Postal Service's lightweight

¹³⁹ See Docket No. ACR2021, Library Reference PRC-LR-ACR2021-1, March 29, 2022.

Competitive products.¹⁴⁰ The cost to the Postal Service of delivering these lightweight parcels is relatively low, but the profit margin associated with lightweight parcels is also low. See Library Reference PRC-LR-ACR2021-1. As a result, measuring the market simply in terms of the number of mailpieces handled could produce a distorted picture of the market that exaggerates the Postal Service's role in it.

Using revenue avoids the foregoing problems, because it is possible to discern the amount of revenue realized by the Postal Service and its competitors respectively with respect to a mailpiece handled by more than one of them, and this relative revenue serves as a proxy for the amount of work actually performed by each market participant. Order No. 4963 at 86. Moreover, and of equal importance, revenue data for all competitors in the market are available and directly comparable, whereas volume data are not uniformly available and would require frequent adjustments due to the assignment issue described above. *Id.* at 19-20; Order No. 4402 at 22-23. For all these

¹⁴⁰ See Docket No. N2021-2, Direct Testimony of Thomas J. Foti on Behalf of the United States Postal Service, June 17, 2021, at 4 (USPS-T-3) (discussing current trends in the lightweight package market). By contrast, UPS "has been focused on shipping more profitable packages, rather than pursuing volume growth." Esther Fung, Wall Street Journal, UPS Earnings Rise as It Ships Fewer Amazon Packages, available at <https://www.wsj.com/articles/ups-earnings-rise-despite-lower-shipping-volumes-11658833646> ("The change in the approach, UPS said, frees it up to focus on gaining new and more profitable customers, including small- and medium-size shippers, and those in healthcare. Residential deliveries typically are less profitable routes since there are fewer packages per stop."); see Paul Ziobro, Wall Street Journal, UPS Ships Fewer Packages as Pandemic Boom Wanes, July 27, 2021, available at https://www.wsj.com/articles/ups-ships-fewer-packages-as-pandemic-boom-wanes-11627393863?st=gznj64stitr4eug&reflink=desktopwebshare_permalink (UPS "is being more selective about which customers it does business with and what items it ships."); Paul Ziobro, Wall Street Journal, Coronavirus Shifts Pricing Power to UPS and FedEx, and They Are Using It July 29, 2020, available at https://www.wsj.com/articles/coronavirus-shifts-pricing-power-to-ups-and-fedexand-they-are-using-it-11596026588?st=yfg9z33b0vng3q4&reflink=desktopwebshare_permalink ("Some consultants say UPS has been willing to let customers ship with other carriers rather than fighting for every last piece of business as has historically been the norm."); Paul Ziobro, Wall Street Journal, UPS Boss Preaches the Power of No, available at https://www.wsj.com/articles/ups-boss-preaches-the-power-of-no-11614335402?mod=article_inline ("The pricing shift highlights two new realities at UPS. Package volume, which the company for years chased to fill its network, was no longer paramount. Instead, UPS could pick better, more profitable deliveries—like heavier packages that cost more to ship or shipments that tend to include multiple packages per stop—and turn away some accounts with lower margins, according to analysts.").

reasons, the Commission continues to find that revenue is a more appropriate measure of market size for competitive postal services than volume.

UPS's assertion that the use of revenue is misleading relies on a theory that the Postal Service underprices its Competitive products. See UPS Reply Comments at 16, 38. However, reliance on such a theory to justify any change to the Commission's proposed approach regarding the appropriate share would be unreasonable. The Commission examined a wide body of evidence and concluded that there is no evidence (either anecdotal or analytical) to support this theory.¹⁴¹ On the contrary, all existing evidence indicates that the Postal Service is competing fairly. Order No. 6043 at 105-09; Order No. 4963 at 49-50.

With respect to UPS's argument that the profits of it and other private competitors in the market for competitive postal services do not necessarily show that the market is competitive, the Commission does not see how UPS could deny that the profitability of the major competitors in the market, including the Postal Service, is relevant to assessing "the prevailing competitive conditions in the market." If there were a competitive deficit in the market arising from the Postal Service's pricing decisions, then one would expect to find evidence of that circumstance reflected in the relative profitability of the various market participants.

After reviewing the available evidence, the Commission continues to find that the state of competition in the market for competitive postal services is healthy and competitive. Since the Commission's last statutorily-required assessment, which ran

¹⁴¹ See Order No. 6043 at 92; Order No. 4963 at 4-12, 49-50, 119-23, 126-32, 134-37, 187; Order No. 4402 at 35-37, 54-68.

through FY 2017, the market for competitive postal services has continued to expand significantly, especially following the outbreak of the COVID-19 pandemic in FY 2020.¹⁴²

Expansion in the market for competitive postal services has continued to be driven by growing demand because of substantial increases in e-commerce sales.

¹⁴² COVID-19 was first detected in humans in approximately December 2019. See *Coronavirus Outbreak Timeline Fast Facts*, available at <https://www.cnn.com/2020/02/06/health/wuhan-coronavirus-timeline-fast-facts/index.html>. For Postal Service reporting purposes, this occurred during FY 2020 Quarter 1 (October 1, 2019 through December 31, 2019). During FY 2020 Quarter 2 (January 1, 2020 through March 31, 2020), COVID-19 was first detected in the United States. *Id.* The Postal Service reported its first confirmed case on February 24, 2020. United States Postal Service, Office of Inspector General, Report No. 20-259-R21, Employee Safety – Postal Service COVID-19 Response, November 20, 2020, at 5, available at <https://www.uspsoig.gov/sites/default/files/document-library-files/2020/20-259-R21.pdf> (OIG Report No. 20-259-R21). In mid-March 2020, approximately 2 weeks before the end of FY 2020 Quarter 2, the World Health Organization declared the outbreak to be a pandemic and the President of the United States issued a national emergency declaration. Proclamation 9994 of March 13, 2020, Declaring a National Emergency Concerning the Novel Coronavirus Disease (COVID-19) Outbreak, 85 Fed. Reg. 15,337-38 (Mar. 18, 2020).

**Table V-2
E-Commerce Sales,
CY 2007–CY 2021**

Calendar Year	E-Commerce Sales (Millions)	Year-over-Year Growth
2007	\$135,877	
2008	\$141,895	4.43%
2009	\$144,900	2.12%
2010	\$169,110	16.71%
2011	\$198,556	17.41%
2012	\$229,295	15.48%
2013	\$259,817	13.31%
2014	\$297,406	14.47%
2015	\$339,062	14.01%
2016	\$388,049	14.45%
2017	\$448,441	15.56%
2018	\$507,628	13.20%
2019	\$571,229	12.53%
2020	\$815,447	42.75%
2021	\$960,444	17.78%

Source: U.S. Census Bureau, Monthly Retail Trade, Quarterly E-Commerce Report Historical Data, available at https://www.census.gov/retail/ecommerce/historic_releases.html.

Table V-2 demonstrates that e-commerce sales have increased by more than 600 percent since Calendar Year (CY) 2007. For over a decade, e-commerce has exhibited double-digit increases in sales. The very large increase in sales for CY 2020, and, to a lesser degree, CY 2021, reflect the extraordinary increase in demand resulting from the COVID-19 pandemic. The continuous growth in demand, fueled by e-commerce sales, has also continued to result in revenue growth for the major competitors in the market for competitive postal services, and hence to significant increases in the size of the market as measured by revenue.

Between FY 2007 and FY 2021, the market for competitive postal services, as measured by revenue, expanded by 50.0 percent.¹⁴³ As shown by Table V-3, the size of the market for competitive postal services has increased every year since FY 2011.

Table V-3
Parcel Delivery Market Growth by Revenue,
FY 2007–FY 2021

Fiscal Year	Postal Service Competitive Product Revenue (Millions)	Competitor Revenue (Millions)	Total Revenue (Millions)
2007	\$7,909	\$77,895	\$85,804
2008	\$8,382	\$76,136	\$84,518
2009	\$8,132	\$64,621	\$72,753
2010	\$8,677	\$63,359	\$72,036
2011	\$8,990	\$66,871	\$75,861
2012	\$11,426	\$69,270	\$80,696
2013	\$13,741	\$70,955	\$84,696
2014	\$15,280	\$73,376	\$88,656
2015	\$16,428	\$77,922	\$94,350
2016	\$18,495	\$81,529	\$100,024
2017	\$20,690	\$86,191	\$106,881
2018	\$19,040	\$77,848	\$96,889
2019	\$19,633	\$81,071	\$100,703
2020	\$24,523	\$88,756	\$113,279
2021	\$26,194	\$102,469	\$128,663

Source: Library Reference PRC-LR-ACR2021-10. The Commission notes that throughout this Order it uses FY 2021 data as the most recent data where FY 2022 data are either not available or have not yet been finalized.

¹⁴³ Docket No. ACR2021, Library Reference PRC-LR-ACR2021-10, March 29, 2022.

Over the last decade, the Postal Service and its competitors have all experienced steady increases in revenue, confirming that all competitors benefited from growth in the market.

Table V-4 displays the market share by revenue for the Postal Service and its major competitors for FY 2007 through FY 2021.

**Table V-4
Market Share by Revenue,
FY 2007–FY 2021**

Fiscal Year	Postal Service Market Share	Competitor Market Share
2007	9.22%	90.78%
2008	9.92%	90.08%
2009	11.18%	88.82%
2010	12.05%	87.95%
2011	11.85%	88.15%
2012	14.16%	85.84%
2013	16.22%	83.78%
2014	17.24%	82.76%
2015	17.41%	82.59%
2016	18.49%	81.51%
2017	19.36%	80.64%
2018	19.65%	80.35%
2019	19.50%	80.50%
2020	21.65%	78.35%
2021	20.36%	79.64%

Source: Library Reference PRC-LR-RM2017-1/3.

As shown in Table V-4, the Postal Service has captured market share since FY 2007, although that growth has steadied over the last 5 years. The Postal Service's market share as measured by revenue was 9.22 percent in FY 2007. Since then, the Postal Service's market share has more than doubled, peaking in FY 2020 at 21.65 percent. In FY 2021, the Postal Service's market share contracted slightly to 20.36 percent. Although the Postal Service's market share has grown, the Postal Service's market share remains relatively modest, and appears to have stabilized over the last 5 years. It has changed very little since the Commission's last statutorily-required review of the appropriate share. See Order No. 4963 at 8. The Postal Service's primary competitors, UPS and FedEx, still capture the vast majority of the market for competitive postal services.

The three aspects of the market's structure that the Commission identified in Order No. 4963—the existence of firm specialization and product differentiation; the use of non-published prices for higher-volume commercial mailers; and the development of “co-opetition” between competitors in the market—all remain equally valid today and continue to be indicative of the existence of healthy competition. As the Commission has explained, a market with a small number of competitors, each of which uses both published and non-published rates, is likely to trend toward an equilibrium point approaching competitive prices, at which each firm produces its products at the least possible cost, and resources are optimally allocated between the various participants in the market. *Id.* at 49. Furthermore, the use of “co-opetition” by market participants to take advantage of each other's specializations results in lower overall costs and improves the productive efficiency of the market. *Id.* at 10.

The major competitors' price increases confirm the health of the market. Table V-5 shows the average annual price increases for all three competitors from CY 2008 to CY 2022. As shown by Table V-5, all three major competitors have implemented

annual price increases as the market has expanded: UPS, FedEx, and the Postal Service each steadily increased prices over the past 15 years.

Table V-5
Average Annual Price Increases,
CY 2008–CY 2022

Calendar Year	Postal Service Price Increase	UPS Price Increase	FedEx Price Increase
2008	5.79%	5.81%	5.81%
2009	5.00%	6.38%	6.38%
2010	3.30%	5.81%	5.38%
2011	3.60%	6.38%	5.90%
2012	4.60%	6.38%	5.90%
2013	8.10%	6.19%	5.90%
2014	2.40%	4.90%	4.37%
2015	3.50%	4.90%	4.90%
2016	9.50%	5.05%	4.90%
2017	3.90%	4.90%	4.37%
2018	4.10%	4.90%	4.90%
2019	7.40%	4.90%	4.90%
2020	3.79%	4.90%	4.90%
2021	5.75%	4.90%	4.90%
2022	5.98%	5.90%	5.90%

Note: After the PAEA bifurcated all Postal Service products into separate categories labeled Market Dominant and Competitive, the Postal Service changed rates of general applicability for a competitive product for the first-time, effective on March 8, 2008. See Docket No. CP2008-1, Order Modifying Mail Classification Schedule, March 3, 2008, at 1-2 (Order No. 63).

Source: Lojistic, 2022 Annual Carrier General Price Increase, available at <https://files.lojistic.com/files/white-papers/2022-UPS-FedEx-GPI.pdf>; Library Reference PRC-LR-RM2017-1/3; workpapers filed in Dockets Nos. CP2020-5, CP2021-28, CP2022-22, CP2022-99. Geometric means were used to develop average increases for the Postal Service, UPS, and FedEx in all calendar years. Geometric means were used to develop average increases for the Postal Service in CY 2008, and for UPS and FedEx in all calendar years. The Commission also presents arithmetic averages for comparison in Library Reference PRC-LR-RM2017-1/3, but the method for calculating the averages does not alter the discussed conclusions.

Table V-6 displays the cumulative price increases for the three competitors for CY 2008 through CY 2012, CY 2013 through CY 2017, and CY 2018 through CY 2022.

Table V-6
Cumulative Price Increases,
CY 2008–CY 2012, CY 2013–CY 2017, and CY 2008–CY 2022

Calendar Years	Postal Service Cumulative Increase	UPS Cumulative Increase	FedEx Cumulative Increase
2008-2012	24.34%	34.78%	33.03%
2013-2018	30.35%	28.77%	26.94%
2018-2022	30.05%	28.23%	28.23%

Note: The Commission use of 5-year blocks of time correspond with the statutory requirement review the appropriate share every 5 years. See 39 U.S.C. § 3633(b). The Commission's first review was in 2012, its second review started in 2017, and the current review began in 2022. See Docket Nos. RM2012-3, RM2017-1, and RM2022-2.

After the PAEA bifurcated all Postal Service products into separate categories labeled Market Dominant and Competitive, the Postal Service changed rates of general applicability for a competitive product for the first-time, effective on March 8, 2008. See Docket No. CP2008-1, Order Modifying Mail Classification Schedule, March 3, 2008, at 1-2 (Order No. 63).

Source: Lojistic, 2022 Annual Carrier General Price Increase; Library Reference PRC-LR-RM2017-1/3; workpapers filed in Dockets Nos. CP2020-5, CP2021-28, CP2022-22, CP2022-99. Geometric means were used to develop average increases for the Postal Service, UPS, and FedEx in all calendar years. Geometric means were used to develop average increases for the Postal Service in CY 2008, and for UPS and FedEx in all calendar years. The Commission also presents arithmetic averages for comparison in Library Reference PRC-LR-RM2017-1/3, but the method for calculating the averages does not alter the discussed conclusions.

While Table V-6 shows the occurrence of some variation in the annual percentage increases among the three competitors, it also confirms that the cumulative price increases have continued to converge. See Order No. 4963 at 11-12. Additionally, the Postal Service's cumulative increase over the last 5 years (CY 2018–CY 2022), as well as over the previous 5 years (CY 2013–CY 2018) exceeded that of either UPS or FedEx. Moreover, the Postal Service has begun to emulate UPS and FedEx by charging higher prices for its Competitive products during peak season, which further shows convergence in pricing.¹⁴⁴

The Postal Service's main two competitors (UPS and FedEx) operate with substantial operating margins. UPS's operating margin has been in the double digits for more than 5 years. From CY 2020 to CY 2021, its adjusted consolidated operating profit grew by more than 50 percent to reach \$13.1 billion.¹⁴⁵ FedEx also had strong operating margins in recent years, with its consolidated operating margin in the fiscal year that ended May 31, 2022 at 6.7 percent, just slightly lower than the 7.0 percent margin in the previous fiscal year.¹⁴⁶ Both UPS and FedEx have implemented aggressive rate increases and pricing changes throughout the last decade, without adverse effect on their businesses, as evidenced by their continued profitability.¹⁴⁷

¹⁴⁴ See, e.g., Docket No. CP2021-127, Order Approving Price Adjustments for Domestic Competitive Products, August 31, 2021, at 1, 3 (Order No. 5973).

¹⁴⁵ United Parcel Service, Inc. Annual Report Pursuant to Section 13 and 15(d), February 22, 2022, at 2, available at <https://investors.ups.com/sec-filings/annual-filings###document-3841-0001090727-22-000007-2> (FY 2021 UPS Annual Report). Changes in adjusted consolidated operating profit are measured as the year-over-year growth in operating profits on a constant currency basis. See FY 2021 UPS Annual Report at 35.

¹⁴⁶ See FedEx 2021 Annual Report, at 1, available at [https://s21.q4cdn.com/665674268/files/doc_financials/annual/2021/389437\(1\)_12_FedEx_AR_WR.pdf](https://s21.q4cdn.com/665674268/files/doc_financials/annual/2021/389437(1)_12_FedEx_AR_WR.pdf). For purposes of FedEx reporting, FY 2022 covers June 1, 2021 through May 31, 2022; FY 2021 covers June 1, 2020 through May 31, 2021. See FedEx Corporation, 2022 Report on Form 10-K, July 18, 2022, at 46, available at https://www.sec.gov/ix?doc=/Archives/edgar/data/1048911/000156459021037031/fdx-10k_20210531.htm (FY 2022 FedEx Form 10-K).

¹⁴⁷ Lojitsic, 2021 Annual Carrier General Price Increase, at 3, available at <https://files.lojistic.com/files/white-papers/UPS-Fedex-General-Price-Increase-History.pdf>.

Additionally, as the Commission has previously noted, ASL has continued to grow its own delivery capabilities. Order No. 6043 at 108. The ability of this relatively new market entrant to successfully compete with the incumbents provides further evidence of healthy competition in the market for competitive postal services.

UPS has noted that the Postal Service has been investing in and has been focused on growing its Competitive business.¹⁴⁸ This behavior by the Postal Service further indicates that the market is competitive and that competition in the market is incentivizing the Postal Service to improve its Competitive offerings or risk losing market share to its competitors. In FY 2019 and FY 2021, the Postal Service did lose some market share to its competitors, which shows that even as the market has expanded, competition for market share has remained strong.

As the Commission explained in Order No. 6043, despite the unpredictable surge in market growth in FY 2020 due to the COVID-19 pandemic, the formula-based approach to determining the appropriate share has functioned as intended. Order No. 6043 at 105.

¹⁴⁸ See, e.g., Initial Comments of United Parcel Service, Inc. on Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products, January 23, 2017, at 28-29 (UPS Order No. 3624 Comments).

Table V-7 below illustrates the recursive calculation of the appropriate share using the formula, starting with an appropriate share of 5.5 percent in FY 2007.

Table V-7
Calculation of Appropriate Share,
FY 2007–FY 2022

Fiscal Year	Appropriate Share for the Current Year (AS_t)	Percentage Change in Competitive Contribution Margin for the Prior Year ($\% \Delta CCM_{t-1}$)	Competitive Growth Differential for the Prior Year (CGD_{t-1})	Appropriate Share for the Following Year (AS_{t+1})
FY 2007	5.5%	N/A	N/A	5.5%
FY 2008	5.5%	0.0%	0.0%	5.5%
FY 2009	5.5%	-5.9%	0.7%	5.2%
FY 2010	5.2%	13.4%	1.2%	6.0%
FY 2011	6.0%	15.7%	1.0%	7.0%
FY 2012	7.0%	-7.9%	-0.2%	6.4%
FY 2013	6.4%	3.7%	2.7%	6.8%
FY 2014	6.8%	5.5%	2.5%	7.3%
FY 2015	7.3%	0.4%	1.2%	7.4%
FY 2016	7.4%	-2.6%	0.2%	7.2%
FY 2017	7.2%	18.1%	1.4%	8.6%
FY 2018	8.6%	1.3%	1.1%	8.8%
FY 2019	8.8%	0.1%	0.4%	8.8%
FY 2020	8.8%	3.5%	-0.2%	9.1%
FY 2021	9.1%	7.2%	3.0%	10.0%
FY 2022	10.0%	5.5%	-1.9%	10.4%

Source: Library Reference PRC-LR-ACR2021-10, folder “PRC-LR-ACR2021-10,” Excel file “PRC-LR-ACR2021-10,” tab “Competitive Growth Differential.”

As Table V-7 shows, since FY 2020 the appropriate share derived from the formula-based approach increased every year, even for FY 2021 and FY 2023, when the Postal Service lost market share to competitors in the previous year, because elevated demand and limited supply in the market for competitive postal services still resulted in increases to the Postal Service's market power. In the formula, the Competitive Contribution Margin represents the Postal Service's absolute market power, while the Competitive Growth Differential reflects the Postal Service's market position. See Section V.B.1.a., *supra*. As a result, the formula considers both changes in the market itself and the Postal Service's standing in the market.

3. The Commission Considered Circumstances Alleged by Commenters to be Relevant Under 39 U.S.C. § 3633(b)

a. Comments

UPS identifies three circumstances that it believes constitute "relevant circumstances" under 39 U.S.C. § 3633(b) that the Commission should consider as part of its appropriate share determination. First, UPS asserts that the Commission should consider the Postal Service's "consistent losses of billions of dollars every year because of its failure to recover institutional costs." UPS Comments at 29-34. According to UPS, the Postal Service's financial losses over the past decade have been driven by its failure to recover institutional costs. *Id.* at 29-31. UPS asserts that the Postal Service's losses "are *not* rooted solely in retiree benefits or workers' compensation[,] [since, among other reasons] the Postal Service has not needed to pay into the retiree health fund since 2012." *Id.* at 30 (emphasis in original). UPS asserts that because "the Commission has held the appropriate share . . . at fairly constant low levels, even as the share covered by market-dominant products has gone nearly straight down, . . . [t]he result is that the respective responsibility of the [Market Dominant and Competitive] lines of business do not add up to anywhere close to 100 [percent], and adopting the proposed formula will simply guarantee that result for another five years." *Id.* at 31-32.

UPS argues, as it has throughout this proceeding, that it is a mistake to believe that the Postal Service is incentivized to maximize profit from Competitive products, and hence to recover as many institutional costs as possible. *Id.* at 33; UPS Reply Comments at 4-12. UPS argues that “while private companies have a strong incentive to set prices so as to maximize profits, governmental entities like the Postal Service have different incentives, such as the incentive to over-expand for non-economic reasons.” UPS Comments at 34.

On the other hand, the Postal Service, the Public Representative, and ASL argue that UPS treats the appropriate share requirement as a ceiling rather than a floor, by focusing in its argument only on the minimum percentage of institutional costs that Competitive products are required to recover and ignoring Competitive products’ actual contribution to institutional costs.¹⁴⁹ The Postal Service, ASL, Dr. Panzar, and PSA argue that the Postal Service’s market conduct has been in line with what would be expected from a profit-maximizing firm.¹⁵⁰ The Postal Service states that its “lack of overall financial sustainability says nothing about whether the Postal Service has incentives to maximize contribution from competitive products; rather, it is a consequence of other factors, the most significant one being a retiree health benefit funding obligation to which private companies like UPS are not subject.” Postal Service Reply Comments at 51 n.44. The Public Representative likewise asserts that “[t]he Postal Service has borne certain institutional costs such as Retiree Health Care benefits costs that no other company or agency is forced to bear[,]” and “Market dominant products’ pricing is and has been constrained to a CPI-U-based price cap, which has limited price increases [on those products]” PR Reply Comments at 8. He also notes that “where UPS has recently realigned its business by dropping customers who

¹⁴⁹ Postal Service Reply Comments at 42; PR Reply Comments at 7; ASL Reply Comments at 8.

¹⁵⁰ Postal Service Reply Comments at 6, 50; ASL Comments at 14; ASL Reply Comments at 9-10; Panzar Decl. at 4; Panzar Reply Decl. at 14-16; PSA Comments at 3.

generate insufficient profits, . . . the Postal Service is prohibited from dropping unprofitable customers.”¹⁵¹

The second “relevant circumstance” that UPS argues the Commission should consider is the nonexistence of a level playing field in the market for competitive postal services. UPS Comments at 34-40. UPS argues that while “the Commission . . . considers only whether the Postal Service has committed anticompetitive conduct that would be actionable under . . . antitrust laws[,] . . . [t]he [PAEA’s] concern with fair competition . . . extends beyond [such conduct].” *Id.* at 35. UPS contends that the PAEA “is concerned about a government agency expanding to compete into the private sector . . . [.]” and that “Congress wanted to prevent the Postal Service from using its status as a government agency with a statutory monopoly over letter mail to compete unfairly against the private sector *at all*” *Id.* at 35-36 (emphasis in original). To that end, “Congress directed the Commission to ensure that the Postal Service’s package delivery business must stand on its own, and cover all of its associated costs.” *Id.* at 36. UPS argues that “[t]he Commission never considers whether the Postal Service is able to avoid covering costs that private sector companies must recover.” *Id.* at 36-37. UPS also disputes the Commission’s finding in Order No. 6043 that the risk of the appropriate share being set too high outweighs the risk of it being set too low, stating that the Commission’s “hypothetical fear” is “dramatically overstated.” *Id.* at 39. UPS asserts that:

Fundamentally, [Order No. 6043] fails to consider the key question: Whether a too-low appropriate share provides the Postal Service with an unfair advantage. Private-sector companies bear costs identical to those the Postal Service classifies as ‘institutional’ . . . [but] [p]rivate-sector competitors . . . would fail to

¹⁵¹ *Id.* (footnote omitted); see ASL Comments at 19 (“UPS has publicly proclaimed a ‘better not bigger’ strategy to maximize profits by turning away all but the most profitable clients and volumes. This may be a winning strategy for UPS shareholders, even if it is being implemented in the midst of severe capacity constraints in the U.S. supply chain, but if anything, UPS’s market share would have been even higher were this not the case.”) (footnote omitted).

have a viable business if they cannot generate sufficient revenues to cover *all* of these costs. When the Postal Service is required to cover only a small amount of these costs with competitive-product revenues, then that plainly is not the level playing field that Congress intended.

Id. at 39-40 (emphasis in original).

The Public Representative disputes UPS's contention that private-sector companies bear costs identical to those UPS classifies as institutional, asserting that "[t]he Postal Service has borne certain institutional costs such as Retiree Health Care benefits costs that no other company or agency is forced to bear." PR Reply Comments at 8. He argues that "Market dominant products' pricing is and has been constrained to a CPI-U-based price cap, which has limited price increases to a rate as low as 2 percent whereas UPS typically raises its rates over 5 percent in any given year." *Id.* In addition, "where UPS has recently realigned its business by dropping customers who generate insufficient profits, and benefitted financially from it, the Postal Service is prohibited from dropping unprofitable customers." *Id.* (footnote omitted). Thus, in the Public Representative's view, "[t]hat the Postal Service is not a private sector company hardly guarantees it a competitive advantage over UPS." *Id.*

The third "relevant circumstance" that UPS argues the Commission should consider is "subsidization." UPS Comments at 40-41. Specifically, UPS argues that "[t]he failure to address whether the Postal Service is accounting for costs of competitive products in a manner consistent with private companies, and thereby protect[ing] fair competition, constitutes a failure to consider whether market-dominant products are effectively subsidizing competitive products." *Id.* at 40. UPS suggests that "subsidization" can occur not only when products fail to cover their attributable (currently defined as incremental) costs, but also "where market-dominant products cover more than their fair share of institutional costs" *Id.* UPS maintains that Market Dominant and Competitive products "are collectively responsible for causing the entirety of

institutional costs, and . . . should be collectively responsible for generating the revenues for covering those costs.” *Id.* at 41 (emphasis omitted).

On the other hand, ASL, Dr. Panzar, and PSA argue that, by definition, products that cover their incremental costs are not subsidized, so the price floors under 39 U.S.C. § 3633(a)(1) and (a)(2), which are both based on incremental costs, are sufficient to prevent any subsidization of Competitive products.¹⁵² ASL, Dr. Panzar, and Pitney Bowes argue that “comparative harm and balance of risks” are relevant circumstances that the Commission should consider as part of its appropriate share determination, inasmuch as the risks of the appropriate share being set too high outweigh the risks of it being set too low.¹⁵³ ASL suggests that the Postal Service’s actual contribution to institutional costs is a relevant circumstance, noting that Competitive product contribution and cost coverage ratios are substantially higher now than they were when Docket No. RM2017-1 was initiated in 2017. ASL Reply Comments at 5, 7.

b. Commission Analysis

UPS attributes the Postal Service’s financial losses since the PAEA’s enactment to the Postal Service’s failure to recover institutional costs. UPS Comments at 29-34. As explained in Order No. 6043, the appropriate share requirement’s purpose is not to protect the Postal Service from financial losses; rather, it is to protect competition in the market for competitive postal services by preventing the possibility of a competitive imbalance arising because of the Postal Service’s pricing decisions with respect to its Competitive products. Order No. 6043 at 62. The Commission previously identified the primary drivers of the Postal Service’s net losses following the PAEA’s enactment as including the PAEA’s Retiree Health Benefits (RHB) prefunding obligation and declines

¹⁵² ASL Comments at 16, 20; ASL Reply Comments at 2; Panzar Decl. at 12, 14; PSA Comments at 2.

¹⁵³ ASL Comments at 23-27; Panzar Decl. at 14-15; Pitney Bowes Comments at 9-10.

in Market Dominant mail volume and overall mail density. See, e.g., Order No. 5763 at 4-11, 76-77, 101-02. These losses have not been driven by Competitive products, and, in fact, revenue from Competitive products has played a significant role in reducing the impact of these losses.¹⁵⁴ Therefore, the Commission does not find such losses relevant to its appropriate share determination.¹⁵⁵

¹⁵⁴ See Docket No. ACR2021, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2021, May 18, 2022, at 49-54 (FY 2021 Financial Report). See also Docket No. ACR2013, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2013, April 10, 2014, App'x A (FY 2013 Financial Report); Docket No. ACR2014, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2014, April 1, 2015, App'x A (FY 2014 Financial Report); Docket No. ACR2015, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2015, March 28, 2016, App'x (FY 2015 Financial Report); Docket No. ACR2016, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2016, March 31, 2017, App'x A (FY 2016 Financial Report); Docket No. ACR2017, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2017, April 5, 2018, App'x A (FY 2017 Financial Report); Docket No. ACR2018, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2018, April 19, 2019, App'x A (FY 2018 Financial Report); Docket No. ACR2019, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2019, May 7, 2020, App'x A (FY 2019 Financial Report); Docket No. ACR2020, Financial Analysis of United States Postal Service Financial Results and 10-K Statement, Fiscal Year 2020, April 26, 2021, App'x A (FY 2020 Financial Report).

¹⁵⁵ UPS notes that the Postal Service defaulted on the majority of its required RHB prefunding obligation, which UPS asserts reduces the role of the RHB prefunding obligation on the Postal Service's losses. UPS Comments at 30. However, as the Commission has explained, the fact that the Postal Service was forced to default on the required RHB prefunding payments did not make them any less of a legal obligation. Order No. 5763 at 116. In April 2022, Congress legislatively cancelled the Postal Service's remaining obligation for unpaid RHB prefunding payments. PSRA § 102.

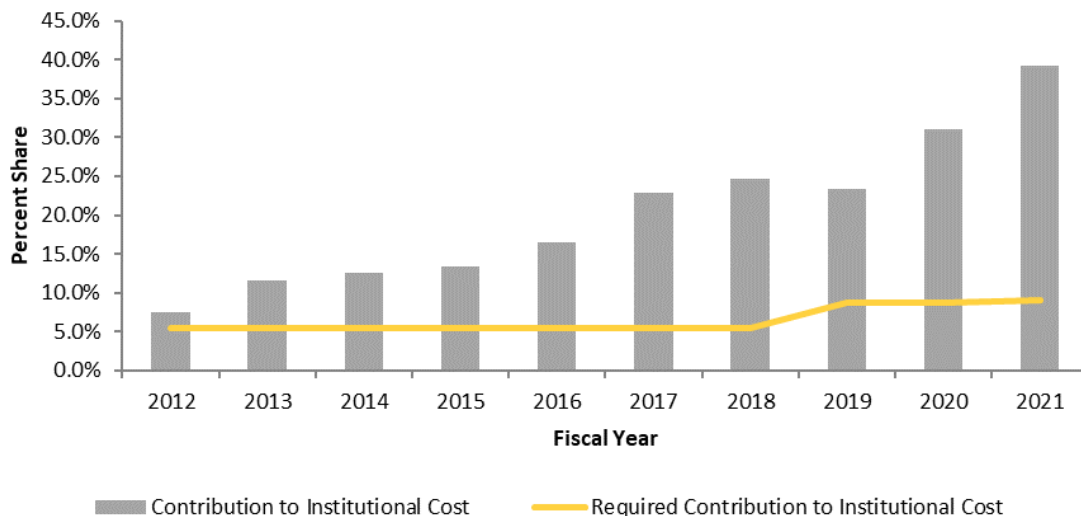
Prior to that time, however, the unpaid RHB prefunding obligation was one of the largest drivers of the Postal Service's losses. Order No. 5763 at 101-02. Before the PSRA was enacted, the Commission authorized the use of above-CPI rate authority to provide the Postal Service with the means to address its RHB prefunding and other retirement obligations. *Id.* at 100-31. The formula pursuant to which such rate authority is calculated was designed to incorporate updates such as Congress's cancellation of the Postal Service's remaining RHB prefunding obligations, through the annual recalculation process, and as a result the above-CPI retirement-based rate authority will be reduced to reflect the removal of that obligation by Congress. Docket No. ACR2021, Determination of Available Market Dominant Rate Authority, March 29, 2022, at 8-9 (Order No. 6130).

UPS also seeks to minimize the role played by workers' compensation expenses in the Postal Service's losses, but as the Commission has explained, the annual non-cash adjustment to the Postal Service's workers' compensation liability has both increased and has tended to fluctuate significantly, which has had a significant negative impact on the Postal Service's ability to generate net income. Order

UPS's statement that "the respective responsibility of the [Market Dominant and Competitive] lines of business do not add up to anywhere close to 100 [percent][,]" (UPS Comments at 32), relies on an incorrect interpretation of the purpose of the appropriate share and misrepresents the reality of Competitive product contribution to institutional costs. As other commenters have noted, UPS repeatedly mischaracterizes a floor as if it were a ceiling. As previously explained (see Section IV.B.2., *supra*), this relies on a misinterpretation of the statute because it conflates the appropriate share requirement, which constitutes a minimum contribution level, with actual Competitive product contribution. Additionally, the statement is misleading because it implies that Competitive products are contributing no more than the minimum required amount to institutional costs and that a significant amount of institutional costs are not being recovered at all. This is false. Competitive product contribution to institutional costs has always exceeded the minimum required appropriate share, and the amount by which it exceeds the appropriate share has grown over time. In FY 2021, the most recent year for which data are available, Competitive products contributed \$13.193 billion, which constituted 39.2 percent of total institutional costs, despite Competitive products making up only 5.97 percent of total mail volume. FY 2021 Financial Report, App'x A. Moreover, in FY 2021, the Postal Service recovered 85 percent of total institutional costs. *Id.*

No. 5763 at 6-7. The non-cash workers' compensation expense includes actuarial revaluations of existing and new cases, initial costs of new cases, and any changes in the discount rate used to estimate the amount of current funds needed to settle all claims in the current year. This is separate from the cash payment made to the U.S. Department of Labor for the current year's cost of medical compensation benefits and an administrative fee. *Id.* at 7 n.14. For examples of recent adverse fluctuations in the non-cash adjustment to the Postal Service's workers' compensation liability, see, e.g., FY 2019 Financial Report at 14, Table II-6; FY 2020 Financial Report at 15, Table II-4.

Figure V-1
Competitive Products' Contribution to Institutional Cost,
FY 2012–FY 2021



Source: FY 2021 Financial Report at 54.

In Order No. 4963, the Commission made detailed findings with respect to the Postal Service's incentives to maximize profit from Competitive products. Order No. 4963 at 60-62. The Commission found that UPS and its declarants' theoretical criticisms of government enterprises in general did not account for the PAEA's bifurcation of regulatory regimes between Market Dominant and Competitive products with respect to pricing. *Id.* at 61. The Commission found that the current structure of the Postal Service and its financial condition create the incentive to maximize profit from Competitive products, because the Postal Service must by necessity look to Competitive products for revenue given the price cap on Market Dominant products and the declines that have occurred in Market Dominant volumes (and hence Market Dominant contribution to institutional costs) since the PAEA was enacted. *Id.* The Commission also found that the Postal Service's conduct has been consistent with this incentive (because the Postal Service has imposed price increases on Competitive

products greater than the rate of inflation and in line with competitors) and has increased the contribution level of Competitive products to institutional costs. Order No. 6043 at 60 n.97; Order No. 4963 at 60-62.

UPS argues that price increases greater than the rate of inflation, without corresponding volume losses, do not necessarily show that the Postal Service has been profit-maximizing with respect to its Competitive products, but rather “suggests that the Postal Service has . . . been pricing its packages at costs that are below what customers would be willing to pay for them—that is, at levels that were not profit maximizing.” UPS Reply Comments at 9-10 (emphasis omitted). UPS argues that the fact that Competitive product contribution has always exceeded Competitive products’ attributable costs and has increased over time “cannot be squared with the Postal Service’s billions of dollars in losses as an enterprise[,]” and “fails to consider how many billions of dollars of costs the Postal Service as an enterprise could shed if it took steps to re-organize the organization in light of the drastic decrease in letter mail volumes that has occurred over the past two decades.” *Id.* at 9 (footnote omitted). UPS argues that the fact that Competitive product contribution has always exceeded the minimum required appropriate share does not necessarily show that the Postal Service has been profit-maximizing with respect to Competitive products because the required contribution level has been “extremely low.” *Id.* at 7-8.

Regardless of whether any one of these speculative arguments by UPS would be persuasive on its own (and they are not), when considered in the totality the available evidence clearly points toward profit-maximizing behavior by the Postal Service with respect to its Competitive products. Enterprise-level losses are not particularly relevant to assessing the Postal Service’s incentives in this regard because most of the Postal Service’s mail volume is Market Dominant, and Market Dominant products operate under a different (and much more restrictive) regulatory regime with respect to pricing. Nor is the amount of money that could be saved because of an efficient reorganization

based on declining Market Dominant volumes relevant. UPS argues that in the absence of Competitive products, “[w]ith ever decreasing letter volumes, if the Postal Service were profit-maximizing, it would take the hard steps required to right-size the business and *decrease* the scope and frequency of its delivery network.” UPS Reply Comments at 27 (emphasis in original). As previously explained, this argument ignores that legal obligations limit the Postal Service’s ability to implement many of the types of hypothetical efficiencies that the “efficient reorganization” UPS speculates about would be premised upon, such as reducing the scope or frequency of the Postal Service’s network. See Section IV.C.2., *supra*.

There is no evidence on this record to indicate that the Postal Service has ever engaged in the kind of pricing behavior UPS accuses it of—engaging in anticompetitive pricing of its Competitive products in order to either expand (or, at a minimum, maintain) its current scale of operations.¹⁵⁶ Finally, as the Commission has found previously,

¹⁵⁶ Over the years, the Commission has examined a wide body of evidence concerning this issue and continues to find no such evidence. See, e.g., Order No. 4402 at 35-37 (finding no evidence that the Postal Service has ever engaged in predatory pricing); *id.* at 54-68; Order No. 4963 at 187 (affirming continuing validity of the FTC’s 2007 finding that the Postal Service operates at a net competitive disadvantage relative to its private sector competitors); Order No. 4963 at 4-12 (assessing conditions in the market for competitive postal services, including overall market size, market share, and competitors’ pricing); Order No. 4963 at 49-50 (finding that the Postal Service has consistently increased Competitive product prices above the rate of inflation); Order No. 4963 at 119-23 (explaining that the Postal Service is not able to simply label costs that should be attributed to Competitive products as institutional and explaining why the postal monopoly does not provide the Postal Service with an unfair competitive advantage with respect to its Competitive products); Order No. 4963 at 126-32 (explaining that the Postal Service has not engaged in predatory pricing, explaining that the Postal Service has increased Competitive product prices greater than inflation every year since CY 2008; explaining that the Postal Service has not underpriced Competitive products featuring last-mile parcel delivery; explaining that the Postal Service’s price increases on Competitive products have been in line with the Postal Service’s competitors; explaining that because of the Market Dominant price cap the Postal Service could not engage in a strategy of underpricing Competitive products and overpricing Market Dominant products; explaining how 39 U.S.C. § 3633(a)(1) and (a)(2) prevent Competitive products from using the Postal Service’s economies of scale and scope to compete unfairly); Order No. 4963 at 134 (explaining that while the Postal Service’s market share has increased it remains relatively low compared to the Postal Service’s competitors); Order No. 4963 at 135-37 (explaining that the market for competitive postal services has grown overall and that the Postal Service has not displaced private competitors; explaining that to the extent the Postal Service has experienced growth in last-mile delivery its competitors also benefit from that via “co-opetition,” which results in lower costs for the Postal Service’s competitors).

given the low volume of Competitive products relative to the Postal Service's overall operations, underpricing Competitive products would not be an effective strategy for expanding the Postal Service's scale. Order No. 6043 at 94 n.143; Order No. 4402 at 74.

With respect to UPS's arguments that the Commission should consider as "relevant circumstances" under 39 U.S.C. § 3633(b) the "nonexistence of a level playing field" and what UPS terms "subsidization," the Commission previously in this Order addressed UPS's arguments regarding the purpose of the appropriate share requirement, including the argument that it is intended to function primarily as a cost allocation provision ensuring the total recovery of all costs "uniquely or disproportionately associated" with Competitive products. See Section IV.B.2., *supra*. The Commission has rejected UPS's argument as to the appropriate share requirement's purpose, and the Commission likewise rejects the related premises that existing circumstances with respect to cost attribution and institutional costs result in a "non-level playing field" or "subsidization." See Sections IV.B.2., IV.C.2., *supra*. UPS has not identified any concrete example of a competitive deficit in the market for competitive postal services other than the fact that institutional costs are not being recovered in the way that UPS would prefer, and what UPS terms "subsidization" does not exist. Incremental costs, which currently form the basis for the price floors under 39 U.S.C. § 3633(a)(1) and (a)(2), are the variable and fixed costs that would be eliminated if a product or group of products were discontinued. Order No. 6043 at 25. This is a standard economic concept that within the field of cost accounting is generally understood to represent the total costs that can be said to have been caused by a product or group of products.¹⁵⁷ By definition, if a product or group of products recovers its incremental costs, it is not being subsidized. UPS's more precise complaint is that

¹⁵⁷ See Panzar Decl. at 20-25. See also 2014 Panzar Report at 2 ("Identifying the relevant economic cost condition is equally straightforward: the costs caused by a product (or group of products) are, by definition, the incremental costs of that product (or group of products)." (emphasis omitted)).

institutional costs—which, by definition, are not caused by any specific product or group of products—are not being recovered in the way that UPS would prefer. UPS would prefer to see an arbitrary percentage of these costs moved into the rate floors for Competitive products, rather than allowing the Postal Service to exercise its pricing flexibility to recover the institutional costs by setting markups on Competitive products that are priced to the market. But given that institutional costs are not caused by Competitive products, debates over how institutional costs are to be recovered have no bearing on the question of whether Competitive products are being subsidized.

As the Public Representative notes, the Postal Service's cost structure is not analogous to a private sector firm in many respects. See PR Reply Comments at 8. The Postal Service operates an integrated processing and delivery network that handles products governed by two separate and distinct ratemaking schemes. The Postal Service's ability to implement price increases with respect to its Market Dominant products, and hence its ability to generate contribution to institutional costs from those products, is sharply circumscribed by a price cap and other statutory and regulatory limitations intended to protect captive Market Dominant mailers. See *generally* 39 U.S.C. § 3622; Order No. 5763 (authorizing the Postal Service to exceed the price cap in certain limited circumstances to recover discrete sources of costs that are not within the Postal Service's control). Hence, the Postal Service's ability to generate contribution to institutional costs from Market Dominant products is limited, but that circumstance is not due to the Postal Service's pricing decisions with respect to its Competitive products. It bears repeating that in FY 2021 Competitive product contribution covered 39.2 percent of institutional costs, despite Competitive products constituting only 5.97 percent of total mail volume. FY 2021 Financial Report, App'x A.

Moreover, the Postal Service, as a federal agency, is subject to legal requirements that private sector companies are not subject to, especially with respect to the level of service the Postal Service must provide and personnel issues such as

compensation and benefits and statutorily-required labor arbitration. The Postal Service operates under a universal service obligation—a broad set of legal mandates that govern the geographic scope of coverage and frequency of delivery, among other aspects of service.¹⁵⁸ To the extent that many institutional costs are network costs incurred in meeting these obligations, they are not analogous to the overhead costs of private-sector firms, which have more flexibility with respect to their operations. The Postal Service is also required by law to provide compensation and benefits to its employees that are in many instances beyond what the market would dictate for a private firm. One of the most notable examples of this was the legal requirement that the Postal Service operated under from CY 2007 to CY 2022 that required it to prefund RHB for future retirees on a compressed 10-year schedule followed by amortization of the remaining unfunded RHB liability, which the Postal Service was ultimately unable to meet.¹⁵⁹ As the Public Representative observes, private sector companies do not face such costs, and hence comparing the Postal Service’s institutional costs to the overhead costs of a private firm is frequently an apples-to-oranges comparison. See PR Reply Comments at 8.

The Commission agrees with the commenters who suggest that comparative harm and balance of risk should be considered as relevant circumstances under 39 U.S.C. § 3633(b), and the Commission has, in fact, long included these as “other relevant circumstances” in its reviews of the appropriate share.¹⁶⁰ In Order No. 6043, the Commission made detailed findings to the effect that the risks of the appropriate

¹⁵⁸ See generally USO Report. See also n.40, *supra*.

¹⁵⁹ See Order No. 5763 at 101-02. See also PSRA § 102 (repealing the requirement that the Postal Service annually prepay future RHB and cancelling all past due prefunding payments).

¹⁶⁰ See, e.g., Order No. 1449 at 12; Order No. 4402 at 50-53; Order No. 4742 at 54-55; Order No. 4963 at 169-70.

share being set too high outweigh the risk of it being set too low.¹⁶¹ UPS does not meaningfully engage with these findings, particularly the Commission's finding with respect to the risks of the appropriate share being set too high. The Commission specifically concluded that an appropriate share that was set too high could confer an unfair competitive advantage on the Postal Service's competitors by permitting them to either: (1) underprice the Postal Service in order to attempt to capture its market share; or (2) take advantage of the Postal Service's inability to reduce its prices in order to cartelize the market. Order No. 6043 at 61, 91-95. UPS does not refute this conclusion or the underlying findings. UPS simply dismisses the weight of the analysis entirely as a "hypothetical fear [that] is dramatically overstated." UPS Comments at 39. However, dismissing these concerns as UPS proposes would be unreasonable given 39 U.S.C. § 3622(b)'s requirement to consider "the prevailing competitive conditions in the market" and the record before the Commission. The weight of the evidence reinforces that the risks of setting the appropriate share too high outweigh the risk of setting the appropriate share too low.¹⁶²

The Commission has also explained in detail why it finds the risk of the appropriate share being set too low to be minimal, including: (1) evidence suggesting that the Postal Service is incentivized to maximize profit from Competitive products and that its conduct has been in line with what would be expected from a profit-maximizing firm; (2) evidence that competition in the market is healthy and competitive; and (3) a lack of evidence of the Postal Service ever having engaged in anticompetitive pricing of its Competitive products. Order No. 6043 at 92-95. UPS fails to refute these findings.

¹⁶¹ Order No. 6043 at 91-95, 104-05. Multiple commenters support these findings. See, e.g., Pitney Bowes Comments at 9-10; ASL Comments at 24, 27; PSA et al. Comments at 6-7.

¹⁶² Where "the Commission's decision depends on 'predictive judgments about the likely economic effects of a rule,' which are 'squarely within the ambit of the Commission's expertise.' ... [t]he [reviewing] court's 'narrow task' is thus 'to ensure that the Commission sufficiently supported its analysis.'" *Nat'l Postal Pol'y Council*, 17 F.4th at 1193 (quoting *Newspapers Ass'n of Am. v. Postal Regul. Comm'n*, 734 F.3d 1208, 1216 (D.C. Cir. 2013)).

Rather, UPS continues to argue that “a too-low appropriate share provides the Postal Service with an unfair advantage . . . [because] [p]rivate-sector companies bear costs identical to those the Postal Service classifies as ‘institutional’ . . . [and] [w]hen the Postal Service is required to cover only a small amount of these costs with competitive-product revenues, then that plainly is not the level playing field that Congress intended.” UPS Comments at 39-40. This argument, however, overlooks the fact that Competitive products’ actual contribution to institutional costs is nearly 40 percent. FY 2021 Financial Report, App’x A. The Commission agrees with ASL that Competitive products’ actual contribution to institutional costs is a relevant circumstance under 39 U.S.C. § 3633(b), and the actual contribution made by Competitive products to the Postal Service’s institutional costs is consistent with the Commission’s prior findings that the risk of the appropriate share being set too low is minimal. The Commission continues to find that the risk of the appropriate share being set too low is outweighed by the risk of it being set too high. Ultimately, UPS’s arguments fail to meaningfully engage with the Commission’s analysis and merely disagree with the outcome of the Commission’s analysis. Notwithstanding UPS’s policy disagreement, the Commission’s final rule is supported by the record and reasonably explained.

4. The Formula is a Reasonable Approach to Setting the Minimum Contribution Requirement

a. Comments

UPS argues, as it has previously in this proceeding, that the formula-based approach is arbitrary and capricious. UPS Comments at 63-68. UPS argues that the 5.5 percent seed value “was . . . artificially low even when first introduced in 2007[,]” and “[s]eeding the current formula at 5.5 [percent] means that the appropriate share will be artificially depressed as long as the formula is used.” *Id.* at 63, 64. UPS argues that the CCM focuses only on whether the Postal Service is overpricing Competitive products and ignores the possibility that the Postal Service could be underpricing Competitive

products. *Id.* at 65. UPS further argues that the CCM “relies on a key input—attributable cost—which is an unreliable gauge for measuring market power[,] [g]iven that attributable costs are an administrative construct, whose measurement relies heavily on petitions to change analytical principles via the regulatory process, so[] changes in attributable costs reflect regulatory legwork rather than genuine changes in economic costs.” *Id.* at 66. Moreover, UPS states that “the inclusion of attributable costs in the CCM component creates a perverse situation where even if competitive products’ attributable costs are increasing, the CCM (and thus the appropriate share) would *fall*—implying an inverse correlation between competitive attributable costs and the competitive share of institutional costs.” *Id.* (emphasis in original).

UPS argues that the CGD is arbitrary because the relative rate at which the Postal Service’s revenue grows compared to private competitors has nothing to do with the extent to which the Postal Service’s Competitive products are held responsible for recovering “their costs.” *Id.* at 67. UPS also argues that the CGD does nothing to promote fair competition, because even if the Postal Service’s market share by volume is increasing rapidly, the CGD will have no effect on the appropriate share so long as Competitive product revenue growth is no greater than private competitors’ revenue growth. *Id.* In addition, UPS argues that the Census data on which the CGD is based includes firms in unrelated industries. *Id.* Finally, UPS argues that it is arbitrary for the CCM and the CGD to be weighted equally. *Id.* at 68. UPS asserts that “depending on how the CCM and CGD are weighted . . . the appropriate share over the years would diverge significantly[,] [and] [g]iven this potential disparity, the Commission’s decision to maintain the equal weighting of the CCM and CGD components remains arbitrary.” *Id.*

The Public Representative, on the other hand, maintains that “the current formula is sound because it combines the desirable properties of simplicity, intuitiveness, [and] economic transparency with a reasonable prospect of stability” PR Comments at 8. He states that the 5.5 percent seed value is reasonable because it is based on

Competitive products' historic contribution to institutional costs at the time the PAEA was enacted. PR Reply Comments at 10. With respect to the CCM, he states that "there is no evidence of predatory pricing behavior by the Postal Service[.]" and "[i]n the absence of any such evidence, UPS's assumption regarding the potential underpricing by the Postal Service of its competitive products is mere speculation. . . ." *Id.* (footnote omitted). With respect to UPS's allegation that the CGD relies on Census data that includes firms in unrelated industries, he states that "unless UPS can demonstrate that the revenues of these firms have grown faster than the revenues of package-delivery firms, the appropriate shares computed by the formula for the last few years are conservatively higher than what they would have been without the non-mail delivery firms." *Id.* at 11. Finally, with respect to the weighting of the CCM and CGD components, the Public Representative states that there is no reason the components should not be equally weighted. PR Comments at 8; PR Reply Comments at 11.

The Public Representative and Pitney Bowes both state that if the Commission is inclined to maintain an appropriate share requirement, they support using the formula-based approach. PR Reply Comments at 16; Pitney Bowes Comments at 13.

The Postal Service proposes a minor technical adjustment to the formula to incorporate subsequent revisions to the Census data used to calculate the CGD. Postal Service Comments at 73-77. Specifically, the Postal Service observes that the Census data that the CGD relies upon are issued quarterly but are subject to subsequent revisions by the Census Bureau. *Id.* at 74. However, the Postal Service notes that the Commission's current approach to calculating the formula-based appropriate share "locks in" the value for a quarter once it has been used and does not incorporate subsequent Census data revisions. *Id.* The Postal Service proposes that quarterly values used in the formula calculation be allowed to "float" until the time that they are entered into the calculation, so that any relevant revisions from the Census Bureau can be incorporated into the data. *Id.* at 75. The Postal Service concedes that, given the

relatively small size of the revisions at issue and the rounding procedures employed, any actual change to the formula-based appropriate share because of this change is likely to be miniscule. *Id.* at 76. Nevertheless, the Postal Service asserts that incorporating the revisions would make the formula calculation more accurate. *Id.* at 76-77.

b. Commission Analysis

The Commission has previously explained the reason for using 5.5 percent as the seed value for the formula.¹⁶³ Specifically, the initial 5.5 percent appropriate share was based on historic contribution at the time the PAEA was enacted, and the purpose of the formula-based approach is to reflect the cumulative effect of developments in the market for competitive postal services on the Postal Service's ability to contribute to institutional costs since the PAEA's enactment. Order No. 4742 at 41. UPS argues that "the seed value of 5.5 [percent] is . . . far removed from the nature of the Postal Service's current business and the secular market trends" UPS Comments at 65. See It must be borne in mind, however, that the appropriate share constitutes a *minimum* contribution requirement. Order No. 4963 at 97-98; Order No. 6043 at 46-47. The appropriate share is not intended to reflect a measure of the amount of institutional costs that are traceable to Competitive products, an amount which, as the Commission has explained, is not possible to quantify. Order No. 6043 at 80-85. Instead, it is intended to reflect the minimal amount necessary to prevent (or correct) any potential market imbalance that could arise because of the Postal Service's pricing decisions. *Id.* at 62. Taking Competitive products' historic contribution to institutional costs at the time of the PAEA's enactment and adjusting that figure to reflect changes in Competitive products' collective capacity to contribute to institutional costs (based on changes in the

¹⁶³ Order No. 4402 at 32; Order No. 4742 at 41-43; Order No. 4963 at 95-98.

Postal Service's market power and market position) is a reasonable approach to setting such a minimum contribution requirement.

UPS argues that the CCM only assesses potential overpricing of Competitive products by the Postal Service, not potential underpricing, which, according to UPS, "is the [PAEA]'s real concern." UPS Comments at 65. The Commission has already addressed arguments as to the appropriate share requirement's purpose. See Sections IV.B.2., IV.C.2., *supra*. The CCM component is designed to measure the Postal Service's market power, and market power expresses itself via above-cost pricing.¹⁶⁴ Understanding the Postal Service's market power in the market for competitive postal services is unquestionably relevant to assessing the prevailing competitive conditions in the market, as it helps the Commission determine whether competition is being preserved and whether the Postal Service has an unfair competitive advantage. Order No. 4963 at 58. If, as UPS alleges, the Postal Service were "underpricing" its Competitive products (by pricing them in a way that deliberately minimized contribution to institutional costs), then the Postal Service could only be doing so to try to gain market share.¹⁶⁵ Market share is measured by the formula's other component—the CGD. If the Postal Service's market share were dramatically expanding, that fact would be reflected in the CGD, and the Commission could then assess whether that expansion was indicative of the type of pricing behavior that UPS alleges the Postal Service to be committing. At present, however, there is no evidence of such behavior reflected in the CGD—despite substantial expansion of the market for competitive postal services since the Commission's last review of the appropriate share, the Postal Service's market share has grown only modestly. In FY 2017, the Postal Service's

¹⁶⁴ See W. Kip Viscusi, Joseph E. Harrington, Jr., and David E. Sappington, *Economics of Regulation and Antitrust*, Fifth Edition, at 90.

¹⁶⁵ UPS refers to this as "over-expanding[ing] for non-economic reasons." UPS Comments at 34.

market share was 19.4 percent.¹⁶⁶ In FY 2020, following the outbreak of the COVID-19 pandemic, it briefly rose to 21.6 percent, before falling back down to 20.4 percent in FY 2021.¹⁶⁷ In total, the Postal Service's market share increased by 1 percentage point since FY 2017. The evidence does not reflect that the Postal Service has ever engaged in the type of pricing behavior described by UPS.

UPS asserts that the CCM incorporates attributable costs, which is an unreliable input because attributable costs are an "administrative construct." Attributable costs are statutorily defined as "the direct and indirect postal costs attributable to . . . product[s] through reliably identified causal relationships." 39 U.S.C. § 3631(b). During the PRA-era, to deal with the "multi-[product] nature of postal operations," and accurately attribute the Postal Service's costs, the Postal Rate Commission, in conjunction with the Postal Service, developed a version of activity-based costing to trace postal costs to the products that caused them. See 2014 Panzar Report at 2. The activity-based costing methodology was developed with "thought and insight from well-known economists including William Baumol, John Panzar, and William Vickrey."¹⁶⁸ Although the definition of an attributable cost has been modified over time to encompass more costs, the fundamental activity-based costing approach has continued into the PAEA-era. See Order No. 6043 at 11-33.

¹⁶⁶ Library Reference PRC-LR-ACR2021-10, Excel file "PRC-LR-ACR2021-10.xlsx," tab "Competitive Growth Differential."

¹⁶⁷ Library Reference PRC-LR-ACR2021-10, Excel file "PRC-LR-ACR2021-10.xlsx," tab "Competitive Growth Differential."

¹⁶⁸ Docket No. RM2016-2, Initial Comments of the United States Postal Service on UPS Proposals One and Two, January 27, 2016. Additionally, with its comments, the Postal Service filed a report by Dr. Michael D. Bradley. See Analysis of UPS Proposals One and Two, and the Supporting Report of Dr. Kevin Neels, January 27, 2016, at 2, available at <https://www.prc.gov/docs/94/94809/Bradley.Analysis.Prop.One.Two.pdf> (citing United States Postal Service, Office of Inspector General, Report No. RARC-WP-12-008, A Primer on Costing Issues, March 20, 2012, at 2, available at https://www.uspsaig.gov/sites/default/files/document-library-files/2015/rarc-wp-12-008_0.pdf).

Although UPS might not always agree with the Commission's application of these concepts to the Postal Service's accrued costs, that does not mean that the Commission's determinations with respect to cost attribution are arbitrary, or that it is arbitrary to use attributable costs in the CCM to assess the Postal Service's market power based on how high it is able to price Competitive products above their attributable costs. Moreover, as the Commission has explained previously, changes in cost attribution methodologies are approved by the Commission only after an opportunity for public comment and if such changes improve the quality, accuracy, or completeness of the data produced (or the analysis of data) or if "such revisions are, in the judgment of the Commission, otherwise necessitated by the public interest."¹⁶⁹ Such being the case, any change to attributable costs resulting from a cost attribution methodology change should result in improving the CCM by improving the accuracy, quality, or completeness of the data underlying the attributable cost input. Order No. 4963 at 68.

UPS asserts that the inclusion of attributable costs in the CCM results in a "perverse situation," because even if Competitive products' attributable costs are increasing, the CCM, and thus, according to UPS, the appropriate share, will fall. UPS Comments at 66. First, this assertion mischaracterizes how the formula works—an increase to Competitive products' attributable costs leads to a net increase in the 39 U.S.C. § 3633(a)(3) price floor. See Section V.A.2.b., *supra*. Second, increases in cost attribution indirectly affect the appropriate share even under the current 5.5 percent appropriate share requirement, and under the formula, incentives to under-attribute costs to Competitive products would be lessened. Order No. 4963 at 69. Third, an increase in the level of attributable costs that the Postal Service's Competitive products

¹⁶⁹ Order No. 4963 at 68; see 39 U.S.C. § 3652(e)(2)(A), (C); 39 C.F.R. § 3050.11(a). Additional grounds for data improvement occur when "the quality of service data has become significantly inaccurate or can be significantly improved," which does not apply here. 39 U.S.C. § 3652(e)(2)(B).

must recover is an outcome that UPS has consistently sought in this and other dockets.¹⁷⁰

With respect to the CGD, UPS argues that the relative growth rate of the Postal Service's competitors has nothing to do with whether Competitive products are covering their costs. UPS Comments at 67. The Commission has already addressed and rejected the argument that the purpose of the appropriate share requirement is for Competitive products to cover "their costs." See Section IV.B.2., *supra*. The relative growth rates of the Postal Service and its competitors are unquestionably relevant to assessing the prevailing competitive conditions in the market.

UPS argues that the CGD is arbitrary because it does not address fair competition, because it "will have no effect on the appropriate share as long as the Postal Service's revenue growth is no greater than its competitors', even if the Postal Service's market share by *volume* is increasing rapidly." UPS Comments at 67 (emphasis in original). UPS suggests that this "creates a perverse incentive for the Postal Service to price competitive products below market." *Id.* However, if the Postal Service were to attempt to strategically lower its prices to prevent the appropriate share from increasing, then Competitive products might not generate enough contribution to meet the appropriate share requirement during the interim period between when the Postal Service lowered its prices and when the corresponding reduction in the

¹⁷⁰ Order No. 4963 at 70. See, e.g., Docket No. RM2015-7, United Parcel Service Comments on Postal Service Proposal Thirteen Regarding City Carrier Street Time Costs, March 18, 2015, at 21-23; Docket No. RM2016-2, Petition of United Parcel Service, Inc. for the Initiation of Proceedings to Make Changes to Postal Service Costing Methodologies, October 8, 2015; Docket No. RM2016-12, United Parcel Service Comments on Postal Service Proposal Four Regarding Proposed Changes in Analytical Principles, October 17, 2016, at 9-11; Docket No. RM2018-6, Comments of United Parcel Service, Inc. on Notice of Proposed Rulemaking on Analytical Principles Used in Periodic Reporting (Proposal Three), June 29, 2018; Docket No. RM2020-9, Petition of United Parcel Service, Inc. for the Initiation of Proceedings to Make Changes to Postal Service Costing Methodologies, May 29, 2020; Docket No. RM2022-1, Initial Comments of United Parcel Service, Inc. on Notice and Order of Proposed Rulemaking on Periodic Reporting, March 25, 2022 (Docket No. RM2022-1, UPS Comments); Docket No. RM2022-1, Reply Comments of United Parcel Service, Inc. on Notice and Order of Proposed Rulemaking on Periodic Reporting, April 29, 2022 (Docket No. RM2022-1, UPS Reply Comments).

appropriate share occurred. Order No. 4963 at 87. Due to the time lag between changes in market conditions and when the appropriate share is updated, changes in the appropriate share would not be instantaneous, making strategic pricing difficult to implement in practice. *Id.* Therefore, the benefits to the Postal Service of maximizing profits are likely to far outweigh any benefit potentially realized from lowering prices in an attempt to decrease the appropriate share. *Id.* Overall, this argument is unpersuasive given the low prospect of a potential reward for, and the considerable risks of, the Postal Service engaging in such behavior.¹⁷¹ Finally, as previously explained, revenue is a better measure of market share than volume. See Section V.B.2.b., *supra*.

UPS alleges that the Census data on which the CGD is based includes firms in unrelated industries, specifically “firms who provide grocery, alcoholic beverage, and restaurant delivery services.” UPS Comments at 67. The Commission addressed this concern previously and found it to be overstated. Order No. 4963 at 80-82. The data that UPS refers to come from the United States Census Bureau’s Quarterly Services Survey (“QSS”), which estimates operating revenues for each service sector of the economy. Order No. 4402 at 24. Revenue data are classified by subsector, with the relevant subsector in this case being North American Industry Classification System (NAICS) Code 492—“Couriers and Messengers.” *Id.* NAICS is designed to classify

¹⁷¹ “[G]iven the low volume of competitive products relative to the Postal Service’s overall operations, underpricing competitive products would not be effective in significantly expanding the Postal Service’s scale.” Order No. 4402 at 74. In addition to external oversight from the Commission in enforcing the provisions of 39 U.S.C. § 3633(a), the Postal Service remains subject to external oversight from Congress, the U.S. Government Accountability Office, and the Postal Service Office of Inspector General. Furthermore, the Governors also oversee Postal Service management. Thus, while the Postal Service lacks shareholders, it does not lack outside oversight to hold the Postal Service accountable for its financial and operational performance.

economic activity by what it terms “establishments.”¹⁷² An establishment is a location from which an “enterprise,” or an individual firm, conducts business. Order No. 4963 at 80. Many enterprises have only one establishment, but large enterprises, including the Postal Service and its major competitors, have many establishments. *Id.* An establishment that has delivery as its primary activity will be classified in one sector; whereas an establishment that has transportation as its primary activity will be classified in another sector—even if both establishments constitute parts of the same enterprise. *Id.* If multiple activities are being carried out at one physical location, NAICS is able to separate the location into separate “establishments” based on the respective work activities being conducted, as long as: (1) no one industry description in the classification includes such combined activities; (2) separate reports can be prepared on the number of employees, their wages and salaries, sales or receipts, and expenses; and (3) employment and output are significant for both activities. *Id.* If the above conditions are not met, then the location in question will be classified based on the primary activity conducted there. *Id.*

As such, NAICS is designed to classify revenue by specific work activity. *Id.* For enterprises for which parcel delivery is only an incidental part of their business, the revenue from parcel delivery is incorporated into NAICS Code 492 to the extent that the enterprise can prepare separate reports on delivery and non-delivery activities. *Id.* It is possible that some retail self-delivery would not be reflected in the Census data, but the amount of such activity is likely to be relatively small, because more substantial enterprises generally use more sophisticated accounting methods that are able to capture the necessary data. *Id.*

¹⁷² Order No. 4963 at 80. See Executive Office of the President, Office of Management & Budget, North American Industry Classification System (2022), at 18-19, available at https://www.census.gov/naics/reference_files_tools/2022_NAICS_Manual.pdf (NAICS 2022 Manual).

Furthermore, the QSS is updated quarterly to reflect new market entrants and is fully redrawn every 5 years.¹⁷³ Thus, while NAICS Code 492 may include some firms at the margins that do not form part of the relevant market and may exclude some firms that do in fact form part of the relevant market, these discrepancies are likely to be small and quickly corrected by the Census Bureau. Order No. 4963 at 81. These small overinclusions and underinclusions may also partially offset each other. *Id.* On balance, then, the Commission continues to find that NAICS Code 492 closely reflects the actual composition of the relevant market, and as a result is not arbitrary.

Finally, UPS continues to argue that assigning equal weight to the CCM and CGD is arbitrary. UPS Comments at 68. The Commission has addressed this concern previously. Order No. 4742 at 43-46. As the Commission has explained, the CCM and the CGD measure separate aspects of the Postal Service's position within the market for competitive postal services and both play critical and equal roles in supporting the formula's ability to capture the criteria set forth in 39 U.S.C. § 3633(b). *Id.* at 43; Order No. 4963 at 102-03. Given that neither component is more significant than the other in capturing the criteria set forth in 39 U.S.C. § 3633(b), the Commission has found it appropriate to weight the components equally. Order No. 4742 at 44; Order No. 4963 at 102-03. From an economic perspective, the assignment of weights at the component level, without unique economic justification, is generally inconsistent with best practice. Order No. 4742 at 44. The Commission has exhaustively addressed comments purporting to provide an economic justification for disparate weighting, and the Commission has explained why it found such comments unpersuasive. Order No. 4963 at 103-07. UPS does not provide any new or different justification in its comments in response to Order No. 6043.

¹⁷³ *Id.* at 81. See United States Census Bureau, Quarterly Services Survey Technical Documentation, available at <https://www.census.gov/services/qss/qsstechdoc.html>.

With respect to the Postal Service's proposed minor technical adjustment to the formula's calculation to incorporate subsequent data revisions by the Census Bureau, the Commission finds that it is a reasonable approach, and the Commission adopts the Postal Service's proposed adjustment. The Commission finds that allowing the quarterly values used in the formula calculation to float until the time they are entered into the calculation to incorporate any relevant data revisions to the quarterly Census Bureau data on which the CGD is based will improve the accuracy of the formula result, even though any changes are likely to be extremely small. The Commission has verified that no relevant data revisions up to the present time would have altered the formula-based appropriate share values for any prior fiscal years, given the small size of the revisions and the rounding to one decimal place, as required by the definitions used in the formula appearing in final 39 C.F.R. § 3035.107(c)(1).

VI. COMMISSION ANALYSIS PURSUANT TO UNCODIFIED SECTION 703(D) OF THE PAEA

A. Introduction

Through enactment of the PAEA, Congress sought to determine whether the Postal Service's competitive products enjoyed any legal advantages over private companies providing similar products. See PAEA § 703; see also S. Rep. No. 108-318, at 29 (2004). Uncodified section 703 of the PAEA directed the FTC to prepare a report identifying federal and state laws that apply differently to the Postal Service's competitive products than to similar products offered by private competitors.¹⁷⁴ The FTC was required to include any recommendations concerning how to end any such

¹⁷⁴ PAEA § 703(a). Section 703 was not codified and is reproduced in the notes of 39 U.S.C.A. 3633. See Federal Trade Commission, *Accounting for Laws that Apply Differently to the United States Postal Service and its Private Competitors*, December 2007 (FTC Report), available at <https://www.ftc.gov/sites/default/files/documents/reports/accounting-laws-apply-differently-united-states-postal-service-and-its-private-competitors-report/080116postal.pdf>.

legal differences that it deemed appropriate and, in the interim, to account for the net economic effect resulting from such differences. PAEA § 703(b). Additionally, section 703(d) of the PAEA directed the Commission, when revising regulations under 39 U.S.C. § 3633, to consider the FTC's recommendations as well as subsequent events that affect the continuing validity of the FTC's net economic effect finding. *Id.* § 703(d).

The FTC issued its report in December 2007, which considered both the implicit subsidies enjoyed by, and legal constraints imposed on, the Postal Service's Competitive products due to the Postal Service's unique legal status.¹⁷⁵ In Chapter IV of its report, the FTC completed its net economic effect analysis by specifically identifying those implicit subsidies and legal constraints that could be quantified in order to calculate any impact on the Postal Service.¹⁷⁶ The FTC calculated the cost of the quantifiable legal constraints and the value of the implicit subsidies and concluded that the Postal Service's unique legal status placed it at a net competitive disadvantage in offering Competitive products relative to private competitors. *Id.* at 64.

During the Commission's second 5-year review of the institutional cost contribution requirement for Competitive products, the Commission proposed revisions to its regulations pursuant to 39 U.S.C. § 3633(a)(3) and (b); therefore, the Commission

¹⁷⁵ FTC Report at 55-77. In its review of the Postal Service's unique legal status, the FTC analyzed laws applicable to the Postal Service due to its status as a governmental entity as well as those disadvantages imposed on, and advantages allowed by the PAEA. *Id.*

¹⁷⁶ *Id.* at 64 n.287. The FTC Report discussed additional implicit subsidies and legal constraints beyond those listed in its net economic effect analysis, but because the additional subsidies and constraints could either not be quantified or the effect on the Postal Service was unclear, the FTC did not include them as part of its final analysis. See *id.* at 1, 50, 54, 56, 64, 89. Among others, the FTC was unable to quantify the implicit subsidies relating to the Postal Service's access to federal funding and eminent domain, preferential customs treatment compared to competitors, immunity from certain conduct under the Federal Tort Claims Act, its exemption from paying federal income taxes, and potential advantages stemming from the Postal Service's letter and mailbox monopolies. *Id.* at 29-37, 47-52, 64. Among others, the FTC was unable to quantify the legal constraints relating to pricing restrictions on competitive products, the costs associated with the Postal Service's Universal Service Obligation, the limited ability of the Postal Service to close post offices, the inability to outsource delivery routes to private carriers, requirements related to retirees, and the restraints on financing and investing. *Id.* at 37-45.

determined that an analysis pursuant to section 703(d) of the PAEA was necessary.¹⁷⁷ “[T]he scope of [the Commission’s] review under section 703(d) is limited to considering whether the laws behind the implicit subsidies and legal constraints quantified by the FTC have changed since the FTC Report’s issuance, and if so, whether those changes affect the continuing validity of the FTC’s estimate of the net economic effect of those laws.”¹⁷⁸

As part of Order No. 4402, the Commission found that only “one law linked to a separately delineated element within the FTC’s calculation that has been amended, thereby constituting an event subsequent to the FTC Report’s issuance that affects the validity of the estimate of the net economic effect” (*i.e.*, international air transportation rate regulation).¹⁷⁹ The Commission removed the cost of the international air transportation rate regulation constraint from the total cost of the legal constraints and updated the FTC’s calculation. See Order No. 4402 at 64. The Commission determined that the updated total cost of the legal constraints continued to be greater than the total value of the implicit subsidies. *Id.* at 65. As such, the Commission found that although the removal of the international air transportation rate regulation constraint altered the overall estimate of the net economic effect, that subsequent event did not undermine the FTC’s overall finding of a net economic disadvantage and that the FTC’s finding remained valid. *Id.* The Commission concluded that the updated range of the implicit subsidies and legal constraints supported its determination that the FTC’s initial

¹⁷⁷ See Order No. 4402 at 54-68. See also Order No. 4742 at 57-58; Order No. 4963 at 170-87.

¹⁷⁸ See Order No. 4402 at 62. See also Order No. 4963 at 173-87; Order No. 6269 at 15.

¹⁷⁹ Order No. 4402 at 63. In the FTC Report, the FTC explained that the Department of Transportation’s regulation of international mail air transport rates cost the Postal Service up to \$98 million more in FY 2006 than if the Postal Service were permitted to independently negotiate the rates on the free market as private companies were, at a value range of \$5 million to \$13 million. FTC Report at 44, 56. In 2008, Congress eliminated the Department of Transportation’s authority to regulate the prices paid by the Postal Service for air transport of international mail, allowing the Postal Service to negotiate terms for international air mail transportation contracts directly with airlines as private companies do. See Pub. L. 110-405, 122 Stat. 4287 (2008). See also FTC Report at 44-45.

estimate of a Postal Service net economic disadvantage remained valid. *Id.* at 67. Additionally, the Commission performed a supplemental analysis by updating the high-end costs associated with both the implicit subsidies and legal constraints based on current competitive product revenue at the time Order No. 4402 was issued.¹⁸⁰

The estimates and conclusions described above were initially affirmed by the Commission as part of Order No. 4742. See Order No. 4742 at 57-58. Subsequently, as part of Order No. 4963, the Commission affirmed its findings related to its section 703(d) analysis from both prior orders. See Order No. 4963 at 187.

Subsequently, the United States Court of Appeals for the District of Columbia Circuit remanded Order No. 4963 to the Commission for further consideration of particular issues identified by the court consistent with the opinion issued in *UPS II*, 955 F.3d 1038. This opinion did not identify any issues related to the Commission's consideration of the FTC Report. On November 18, 2021, the Commission issued Order No. 6043, which not only addressed the issues identified by the court, but also initiated the Commission's third 5-year review of the institutional cost contribution requirement for Competitive products and invited public comment by February 25, 2022 (for initial comments) and by March 25, 2022 (for reply comments). Order No. 6043 at 130-31. The Commission stated that it had "reviewed its findings from Order No. 4402

¹⁸⁰ The FTC estimated the low-end cost impact of the quantifiable implicit subsidies and legal constraints on competitive products by using competitive products' 5.5-percent mandatory contribution to institutional costs, which was the appropriate share mandated at the time of the FTC's review. See Order No. 4402 at 65. At the time Order No. 4402 was issued, Competitive products' appropriate share of institutional costs was 5.5 percent. Thus, the Commission found it unnecessary to update the low-end figures estimated by the FTC. See *id.* at 65-66.

The FTC's estimate of the high-end cost impact of the quantifiable implicit subsidies and legal constraints on competitive products was based on competitive product revenue, which at the time of the FTC's review was 13 percent of total Postal Service revenue. See Order No. 4402 at 66 (citing FTC Report at 55-57). However, the Commission found it appropriate to update the high-end cost figures of the quantifiable implicit subsidies and legal constraints based on the best available Competitive product revenue totals at that time. See *id.* at 66-67. At the time Order No. 4402 issued, the best available figure was 29.69 percent, because Competitive products made up 29.69 percent of total Postal Service revenue in FY 2017. Library Reference PRC-LR-ACR2021-1.

with respect to the FTC Report, and conclude[d] that no further events have occurred subsequent to the issuance of Order No. 4402 that would affect the ongoing validity of those findings.” *Id.* at 109 n.165.

After the issuance of Order No. 6043 and the expiration of the comment period established therein, the PSRA was enacted on April 6, 2022. See PSRA. Among other things, the PSRA requires Postal Service Health Benefits plans to participate in Medicare Part D, which would allow those plans to receive subsidies related to prescription drugs. See 5 U.S.C. § 8903c(h). This new requirement is relevant to the Commission’s analysis because, in its report, the FTC specifically identified and included the Postal Service’s inability to access subsidies offered to private employers under the Medicare Part D program in its calculation of the total legal constraints. See FTC Report at 38-39, 56.

Accordingly, on September 7, 2022, the Commission issued Order No. 6269, which found that the Medicare Part D legal constraint had been amended, thereby constituting an event subsequent to the FTC Report’s issuance that affects the validity of the estimate of the net economic effect. Order No. 6269 at 8. The Commission found that, although the subsequent event altered the overall estimate of the net economic effect, it did not alter the FTC’s overall finding of a net economic disadvantage. *Id.* at 10. Thus, the Commission determined that the FTC’s finding of a Postal Service net economic disadvantage continued to be valid.¹⁸¹

¹⁸¹ Order No. 6269 at 10. Similar to Order No. 4402, as part of Order No. 6269, the Commission provided a supplemental analysis that updated the range of costs associated with the implicit subsidies and legal constraints, using the same methodology that the FTC used to develop the range representing the net economic effect on Competitive products. See *id.* at 10-14. The Commission found that the updated range of the implicit subsidies and legal constraints in its supplemental analysis did not alter the Commission’s determination that the FTC’s initial estimate of a Postal Service net economic disadvantage remains valid. *Id.* at 14.

The Commission invited comments regarding its analysis. See Order No. 6269 at 15. No comments were filed contesting the Commission’s interpretation of the scope of its section 703(d) review. Generally, ASL, Pitney Bowes, PSA, the Public Representative, and the Postal Service agree with the analysis presented by the Commission in Order No. 6269.¹⁸² UPS argues that the Commission should consider the PSRA’s termination of the RHB prefunding requirement by altering the FTC-quantified Wage Premium legal constraint whereas the Postal Service replies that UPS offers no valid basis to justify deviating from the analysis presented in Order No. 6269. *Compare* UPS 703(d) Comments *with* Postal Service 703(d) Reply Comments.

B. Comments

UPS argues that the enactment of the PSRA “conferred a material economic benefit on the Postal Service,” which ended the Postal Service’s RHB prefunding requirement. UPS 703(d) Comments at 2. Although the RHB prefunding was not included by the FTC as a quantifiable legal constraint, UPS contends that FTC “considered” it by mentioning it. *Id.* at 3 (citing FTC Report at 38-39). UPS asserts that the Commission should consider the impact of the PSRA’s removal of the pre-funding requirement by altering the FTC-quantified Wage Premium legal constraint to be consistent in the Commission’s treatment of the FTC Report. *Id.* at 2-3.

UPS notes that Order No. 6269 deducted the costs presented by the FTC, which represent the amount the Postal Service previously paid above what private-sector competitors pay and, as UPS asserts, is funded by general tax revenues that the Postal Service does not pay. *Id.* at 2 n.2. UPS states that a “fulsome accounting would also examine the benefit the Postal Service enjoys from having its retirees partake in Medicare Part D while not paying tax revenues that provide the funding for Medicare

¹⁸² See ASL 703(d) Comments; Pitney Bowes 703(d) Comments; PSA 703(d) Comments; PR 703(d) Comments; Postal Service 703(d) Comments.

Part D.” *Id.* UPS argues that the net economic effect of the passage of the PSRA exceeds the range indicated by Order No. 6269. *Id.* at 1-2 (citing Order No. 6269 at 13, Table III-4). UPS contends that the Commission should account for this change as part of its section 703(d) analysis, which it values at \$4 billion annually. *Id.* at 2-3. UPS presents a table and asserts that after reducing the Wage Premium legal constraint and revising the total range, “the Postal Service may be operating at a net advantage relative to its private sector competitors.” *Id.* at 4-5.

The Postal Service disagrees with UPS’s argument that the FTC’s awareness of the RHB prefunding obligation places that obligation within the scope of this proceeding, because the obligation is neither a legal constraint nor an implicit subsidy quantified by the FTC. Postal Service 703(d) Reply Comments at 2. The Postal Service counters that the “more ‘fulsome accounting’” demanded by UPS would require additional analysis than described by UPS. *Id.* at 4. The Postal Service explains that “all the ways in which the Postal Service’s retiree health benefits program, and how [it] will integrate with Medicare beginning in calendar year 2025 with the implementation of the new postal health plans, imposes burdens that differs from the private sector.” *Id.* The Postal Service observes that the PSRA does not allow full Medicare integration, like private sector entities, and thus the Postal Service “will still bear RHB costs that the private sector does not.” *Id.* at 4-5.

The Postal Service states that several “distortions” appear in UPS’s comments. *Id.* at 2 (quoting UPS 703(d) Comments at 2). The Postal Service clarifies that the PSRA relieved it of the obligation to *prefund* RHB payments but did not relieve the Postal Service’s obligation to pay such benefits.¹⁸³ The Postal Service also states that UPS conflates the un-quantified RHB prefunding requirement with the quantified Wage

¹⁸³ Postal Service 703(d) Reply Comments at 2 (noting that 5 U.S.C. § 8906(g)(2) still requires that the government contribution to RHB for postal annuitants must first be paid from the Postal Service RHB Fund, and then by the Postal Service if the fund is exhausted).

Premium legal constraint. Postal Service 703(d) Reply Comments at 2-3. The Postal Service explains that the FTC's mention of the RHB prefunding requirement and its discussion on the Wage Premium legal constraint are done separately, where one is discussed in terms of differences in employee benefits and the other is discussed in terms of differences in salary. *Id.* at 3. It further elaborates that the Wage Premium legal constraint "never included" the RHB prefunding amount in its calculation and was only based on wages that were estimated from time periods before the RHB prefunding requirement was established by the PAEA. *Id.* at 3-4. Thus, the Postal Service asserts that it would be "plainly unreasonable" to subtract RHB prefunding amounts from the Wage Premium legal constraint "that were never initially included in that component." *Id.* at 4.

C. Commission Analysis

Several commenters agreed with the Commission's findings in Order No. 6269 regarding the scope of a Commission review pursuant to section 703(d), the removal of Medicare Part D as a subsequent event, and the Commission's conclusion that the FTC Report's finding of a Postal Service net economic disadvantage remains valid.¹⁸⁴ The Commission rejects UPS's arguments to consider the PSRA's termination of the RHB prefunding requirement by altering the FTC-quantified Wage Premium legal constraint because UPS offers no valid basis to justify deviating from the analysis presented in Order No. 6269.

¹⁸⁴ PSA 703(d) Comments at 2; Postal Service 703(d) Comments at 2, 2-3; Pitney Bowes 703(d) Comments at 2, 3; ASL 703(d) Comments at 2; PR 703(d) Comments at 6; Postal Service 703(d) Comments at 2-3.

The Commission disagrees that a “fulsome accounting . . . [to] examine the benefit the Postal Service enjoys from having its retirees partake in Medicare Part D while not paying tax revenues that provide the funding for Medicare Part D,” is necessary or appropriate to perform in the section 703(d) review. UPS 703(d) Comments at 2 n.2. The Commission’s review is limited to considering whether the laws behind the implicit subsidies and legal constraints quantified by the FTC have changed since the FTC Report’s issuance, and if so, whether those changes affect the continuing validity of the FTC’s estimate of the net economic effect of those laws.” Order No. 6269 at 4 (quoting Order No. 4402 at 62). No basis has been provided to expand the scope.¹⁸⁵

The Commission disagrees with UPS’s contention that the elimination of the prefunding obligation is within the scope of the Commission’s 703(d) review in this proceeding because the FTC “considered” it. UPS 703(d) Comments at 3. The FTC Report displays awareness of the prefunding obligation; however, the FTC Report did not quantify this obligation in estimating the implicit subsidies and legal constraints

¹⁸⁵ See Order No. 4402 at 62-63; Order No. 4963 at 173-87. In reaching this interpretation of section 703(d), the Commission considered the alternative interpretations offered by commenters and determined that the commenters “provide[d] no statutory basis for their stance that a subsequent event under section 703(d) should be viewed more broadly.” Order No. 4963 at 187. The plain meaning of the terms and phrases used in the text of section 703(d) unambiguously limits the scope of the Commission’s review to considering whether the laws behind the implicit subsidies and legal constraints quantified by the FTC have changed since the FTC Report’s issuance, and if so, whether those changes affect the continuing validity of the FTC’s estimate of the net economic effect of those laws. See Order No. 4402 at 61-62. This interpretation is reinforced by the title of section 703, which is “Study on Equal Application of Laws to Competitive Products.” Additionally, the structure of section 703, begins with subsection (a) titled “In General” to focus the scope of the FTC report and ends with subsection (d) to focus the matters for the Commission’s consideration. Thus, the purpose of section 703 reflects a clearly limited scope. See Order No. 4402 at 62. Furthermore, to the extent that any ambiguity exists with respect to the scope of section 703 (which no party has argued), then the legislative history confirms section 703’s focus upon any potential “discriminatory laws” (S. Rep. No. 108-318, at 29 (2004)) and “disparities in legal treatment” (H. Rep. No. 109-66, pt. 1, at 63 (2005)) rather than a broader scope.

quantified by the FTC and to develop its net economic effect finding.¹⁸⁶ Thus, the PSRA's termination of the RHB prefunding requirement does not qualify as a "subsequent event" pursuant to section 703(d) and consideration is outside the scope of the Commission's 703(d) analysis.

The Commission also disagrees with UPS's assertion that, despite the FTC's inability to quantify the cost of the RHB prefunding requirement, the Commission should nonetheless consider it to be "consistent in its treatment of the FTC Report." UPS 703(d) Comments at 3-4. The Commission's prior treatment of changes in the law has been limited to implicit subsidies and legal constraints quantified by the FTC (and thus used to calculate its net economic finding). See Order No. 4402 at 63-65; Order No. 6269 at 8-9. The removal of the cost of the Medicare Part D legal constraint from the total legal constraints that remained from the FTC Report detailed in Order No. 6269 is consistent with the Commission's prior treatment of the change in the law relating to the international air transportation rate regulation legal constraint. See Order No. 4402 at 63-65; Order No. 6269 at 8-9. Both constraints were quantified and used in calculating the range of net economic disadvantage in the FTC Report. See FTC Report at 38-39, 44-45, 56. Therefore, the Commission considers these to constitute subsequent events that affect the continuing validity of the FTC's net economic effect finding. PAEA § 703(d). Any attempt to investigate additional benefits or costs that result from the PSRA's removal of the Medicare Part D legal constraint would be inconsistent with this prior treatment.

Moreover, the Commission examines what UPS identifies as an association between the unquantified RHB prefunding requirement and the quantified Wage Premium legal constraint. UPS contends that the discontinuance of the RHB prefunding

¹⁸⁶ Compare FTC Report at 38-39, with *id.* at 56-57. The FTC Report mentions *several* additional implicit subsidies and legal constraints (*e.g.*, potential advantages stemming from the Postal Service's letter and mailbox monopolies, as well as the costs associated with the Postal Service's Universal Service Obligation), that the FTC did not use to develop its net economic effect finding. See n.180, *supra*.

requirement should offset the FTC-quantified Wage Premium legal constraint. UPS 703(d) Comments at 3. UPS proposes this based on the notion that the Postal Service can now “provide non-wage retirement health benefits for which it no longer bears the costs,” which it appears to assert could lower expenses associated with competing for employees. *Id.*

However, as the Postal Service observes, these two legal constraints are unrelated. Postal Service 703(d) Reply Comments at 3. The FTC Report’s mention of the RHB prefunding requirement and its discussion on the Wage Premium legal constraint are separate. *Id.* The FTC acknowledges the RHB prefunding requirement, insofar as explaining how the Postal Service differs from private sector employers in terms of employee benefits. *Id.*; FTC Report at 38-39. On the other hand, the FTC quantifies the wage premium, which relates to the higher salary paid to Postal Service workers versus private sector employees. Postal Service 703(d) Reply Comments at 3; FTC Report at 39, 56, 65. The Commission agrees. Nothing in the FTC Report indicates that these two legal constraints are related to each other.

It would be unreasonable to subtract the estimated RHB prefunding amount (\$4 billion annually) from the Wage Premium legal constraint as UPS suggests, because it was never included in the FTC’s calculation of the Wage Premium legal constraint in the first place. See Postal Service 703(d) Reply Comments at 3-4. The FTC Report did not include RHB prefunding costs as part of its calculation of the total legal constraints. See FTC Report at 38-39, 55-56. The FTC Report explains that “[t]his [wage premium legal constraint] is calculated based on a 21.2 percent wage premium (see *supra*, at 39) applied to all bargaining employees, whose total FY 2006 compensation was \$31,824 million.” *Id.* at 56 n.268. The plain language is inconsistent with UPS’s claim that this

wage premium figure includes the cost of RHB.¹⁸⁷ Thus, it is a *wage* premium rather than a total *labor cost* premium as UPS incorrectly implies.

Finally, even if UPS were correct that the Wage Premium legal constraint estimated by the FTC included RHB prefunding costs (which it is not), it would not be appropriate to use the FY 2021 cost, as UPS does, to adjust the FY 2006 costs calculated by FTC. This is because the FY 2006 equivalent of current year RHB costs was \$1.6 billion, not the (FY 2021) \$4 billion used by UPS.¹⁸⁸

For the reasons discussed above, the Commission declines to alter the FTC's estimated cost of Medicare Part D or deduct an unverified estimation of the cost of the RHB prefunding requirement from the Wage Premium legal constraint identified by the FTC. Thus, the Commission continues to find that the FTC's initial estimate of a Postal Service net economic disadvantage remains valid. Ultimately, although the Commission has updated its supplemental analysis to "take into account . . . subsequent events that affect the continuing validity of the estimate of the net economic effect" (PAEA § 703(d)), the Commission relies on the criteria appearing in 39 U.S.C. § 3633(b) to develop its dynamic formula-based approach. The FTC Report, as

¹⁸⁷ The Wage Premium legal constraint cost quantified by the FTC consists of the premium in wages paid to bargaining-unit employees; this constraint does not include non-bargaining employees' wages or other compensation, or RHB costs. The wage premium of 21.2 percent used by the FTC was initially calculated in connection with arbitration proceedings predating the PAEA's imposition of the prefunding obligation. See FTC Report at 39 (citing Comments of the United States Postal Service to the Federal Trade Commission Concerning USPS Study, Project No. P071200, August 6, 2007, at 13 n.39 (citing Statement of Michael L. Wachter, Before the President's Commission on the United States Postal Service, April 29, 2003, at 4 (citing Stephen B. Goldberg, Chairman, "Supplemental Opinion Dealing with Economic Issues" Interest Arbitration Proceedings, United States Postal Service and APWU, January 11, 2002, at 203))).

¹⁸⁸ See (1) FY 2006 Cost and Revenue Analysis (CRA) report, PRC Version (2) FY 2006 CRA Model, USPS and PRC versions (3) Transportation Excel Files (4) FY 2006 "B" workpapers, USPS and PRC versions (5) Cost Segment 3 accrued cost pools, USPS and PRC versions, available at <https://www.prc.gov/dockets/document/57163>; ZIP file "FY2006_CRA_model-USPS_and_PRC_versions.zip"; Excel file "FY06PRC.CRpt.xls." Prior to the PAEA, the Postal Service paid only the claims and administrative costs incurred each year; so, the costs, then referred to as "Annuitant Health Benefits" were not really comparable to the "current year" costs for which UPS seeks to adjust.

updated by the Commission's supplemental analysis, merely serves to confirm the Commission's analysis of all relevant circumstances. See Chapter V., *supra* (examining all relevant circumstances); Order No. 6043 at 71-109 (same).

VII. COMMISSION CONSIDERATION OF SPECIFIC COSTS RAISED BY COMMENTERS

A. Background

Order No. 6043 addressed allegations by UPS that specific types of costs were uniquely or disproportionately associated with Competitive products and were being inappropriately treated as institutional costs (rather than being attributed to Competitive products). Order No. 6043 at 109. This discussion included costs associated with new vehicle purchases, city carrier assistant costs, headquarters expenses, NSA transaction costs, data processing supplies and services, Inspection Service field support, building projects expenses, "U.S. Postal Service boxes," supply personnel, city carrier street time, and package processing and delivery technology. *Id.* The Commission found that many of these costs were significantly less than the formula-based appropriate share amount and that attributing them to Competitive products would not have a material effect on Competitive profitability. *Id.* at 109-10. Nevertheless, to clarify the record, the Commission explained why each of the costs raised by UPS was either already attributed to Competitive products,¹⁸⁹ or was properly classified as institutional. *Id.* at 110.

¹⁸⁹ Due to their role as the mathematical base for the 39 U.S.C. § 3633(a)(3) price floor counting them again (as proposed by UPS) would be unnecessary and inappropriate. See Section V.A.1.a., *supra*; Order No. 6043 at 74-80.

The Commission explained how its explicit consideration of each of the types of costs raised by UPS more than satisfied the requirements of 39 U.S.C. § 3633(b) and the instructions of the D.C. Circuit in *UPS II*. *Id.* As required by the court, the Commission explained how it considered “all costs uniquely or disproportionately associated with competitive products in setting the appropriate share, even if it has already accounted for those costs under § 3633(a)(1) and (a)(2).” *UPS II*, 955 F.3d at 1051. However, the court did not decide whether any given cost was, in fact, uniquely or disproportionately associated with Competitive products, and the Commission explained that many costs do not fit that definition, as clarified by the court. Order No. 6043 at 110.

Furthermore, even for costs that do meet the definition of being uniquely or disproportionately associated with Competitive products, the Commission is only required to consider them in determining what the appropriate share should be; there is no requirement that they must be accounted for in any specific way. *Id.* Neither the PAEA nor *UPS II* require that any alteration be made to the appropriate share requirement to reflect such costs. *Id.*; see *UPS II*, 955 F.3d at 1051. After considering the costs identified by UPS, the Commission found that alterations to its proposed dynamic formula-based approach were neither necessary nor appropriate. Order No. 6043 at 110. This finding was based on the Commission’s expertise in postal costing, economics, and policy. See *id.* The Commission invited further public comment on whether the Commission should consider any additional costs.¹⁹⁰

¹⁹⁰ Order No. 6043 at 110. The Commission also stated that if UPS contended that any of the costs it had identified should be attributed to Competitive products, either individually or collectively, then UPS could petition the Commission to initiate a rulemaking proceeding in which UPS could propose an alternative costing methodology for the Commission to consider. *Id.* at 110-11. The Commission’s rules allow any interested party to petition the Commission to initiate proceedings to consider proposals to change an accepted analytical principle. See 39 C.F.R. § 3050.11(a). The Commission may also initiate such proceedings *sua sponte*. *Id.*

Comments received in response to Order No. 6043 can be grouped into two general categories: those pertaining to costs that the Commission specifically addressed in Order No. 6043; and those raising new types of costs that were not addressed in Order No. 6043.

B. Costs Specifically Addressed in Order No. 6043

UPS disputes the Commission's finding in Order No. 6043 that none of the specific costs identified by UPS are uniquely or disproportionately associated with Competitive products (*see generally* Order No. 6043 at 109-129) maintaining that "[w]hen specific drivers of institutional costs are considered, there is an obvious and meaningful relationship between many types of institutional costs and competitive products." UPS Comments at 17. UPS specifically takes issue with the Commission's findings with respect to new vehicle purchases; city carrier assistant costs; headquarters and management costs; supply personnel and city carrier street time; and package processing and delivery technology.

The Public Representative, ASL, Pitney Bowes, and Dr. Panzar all concur with the Commission's findings from Order No. 6043 with respect to the specific costs identified by UPS.¹⁹¹ ASL and Dr. Panzar argue that the issues raised by UPS are questions of cost attribution that have no relevance to the Commission's appropriate share determination. ASL Comments at 31-32; Panzar Decl. at 25. The Public Representative, ASL, Dr. Panzar, and Pitney Bowes all emphasize that any such costs are so small as to be immaterial relative to either the formula-based appropriate share or Competitive products' actual contribution to institutional costs.¹⁹² UPS counters that these costs are only "specific examples." UPS Reply Comments at 20. UPS states that

¹⁹¹ PR Comments at 9-10; ASL Comments at 2-3, 30-32; ASL Reply Comments at 3-4; Panzar Decl. at 28-29.

¹⁹² See PR Comments at 9-10; ASL Comments at 31-32; Panzar Decl. at 29; Pitney Bowes Comments at 11.

it “did not engage in a comprehensive exercise to identify *all* institutional costs that are uniquely or disproportionately associated with competitive products . . . ,” because that “is the job of the Commission and/or the Postal Service[]” and “[i]t is unreasonable to impose th[e] obligation on UPS alone.” *Id.* at 20-21 (emphasis in original).

The Commission has considered each of these costs, and, as discussed in greater detail below, concludes that, except for those that are attributed to Competitive products, they are not uniquely or disproportionately associated with Competitive products. For each of these costs, UPS has failed to offer a meaningful rebuttal to the Commission’s conclusions from Order No. 6043 or any reasoned basis to alter the formula-based approach. The Commission’s expert judgments on these matters warrant judicial deference because they constitute the “agency’s reasoned judgments about technical questions within its area of expertise” that are “reasonable” and “reasonably explained”. *UPS I*, 890 F.3d at 1066 (internal quotations omitted).

Moreover, even if these cost categories were deemed “uniquely” or “disproportionately” associated by a federal court reviewing this matter, it would be inappropriate to alter the formula-based approach to account for these cost categories because the Commission’s formula-based appropriate share is more than sufficient to ensure coverage. Many of these cost categories are significantly less than the formula-based appropriate share (and are significantly less than Competitive products’ actual contribution to institutional costs).

Generally, cost attribution continues to improve given recent methodological changes. In Docket No. RM2022-13, for example, the Commission recently approved an update to the Postal Service’s methodology for distributing peak season highway transportation costs to products that would improve the quality, accuracy, and completeness of sampling of peak season highway routes and of developing a separate

distribution key for peak season highway costs in the first quarter of the fiscal year.¹⁹³ In Docket No. RM2021-1, the Commission recently approved updates to the variabilities for certain types of purchased highway transportation contracts to reflect recent operational changes.¹⁹⁴ In Docket No. RM2021-7, the Commission recently approved replacement of the system used to distribute delivery costs for SPRs with a revised system that replaces manual sampling with scan data from relevant parcel tracking and employee timekeeping databases.¹⁹⁵ The Commission strives, as always, to extend cost attribution to the greatest extent technically feasible without sacrificing accuracy in doing so. Any interested party may file a petition for the Commission to consider a proposal to change an accepted analytical principal regarding any type of cost.¹⁹⁶

1. New Vehicle Purchases

a. Prior Commission Findings

The Postal Service is currently in the process of replacing its fleet of delivery vehicles. Order No. 6043 at 114. In response to allegations by UPS that the costs associated with these new delivery vehicles are uniquely or disproportionately associated with Competitive products, the Commission explained that under the current costing methodology, vehicle depreciation costs are the sum of depreciation costs for four different cost components representing different types of vehicle activity: city

¹⁹³ Docket No. RM2022-13, Order on Analytical Principles Used in Periodic Reporting (Proposal Six), November 3, 2022, at 5 (Order No. 6322).

¹⁹⁴ Docket No. RM2021-1, Order on Analytical Principles Used in Periodic Reporting (Proposal Seven), October 6, 2021 (Order No. 5999).

¹⁹⁵ Docket No. RM2021-7, Order on Analytical Principles Used in Periodic Reporting (Proposal Four), September 30, 2021 (Order No. 5991).

¹⁹⁶ 39 U.S.C. § 3652(e)(2)(A), (C). Additional grounds for data improvement occur when “the quality of service data has become significantly inaccurate or can be significantly improved[.]” which does not apply here. 39 U.S.C. § 3652(e)(2)(B).

delivery vehicles (used for both letter routes and SPRs); “vehicle service drivers;” vehicles used for rural delivery; and “other vehicles.”¹⁹⁷

Depreciation costs for “other vehicles” are considered entirely institutional because such vehicles are used for administrative purposes, not for mail transportation or delivery, and therefore are not specific to any particular mail product or group of products. Order No. 6043 at 115. In FY 2020 these made up 8.0 percent of total vehicle depreciation costs. *Id.* The other three categories are related to mail transportation or delivery and are attributed in the same proportions as the labor costs for the carriers operating the vehicles. *Id.* Because vehicles incur annual depreciation costs whether they are used actively or simply remain parked in a lot, vehicle depreciation costs do not vary proportionally with delivered volume. *Id.*

Depreciation costs for city delivery vehicles are attributed based on the attribution of city carrier labor costs. *Id.* For city carriers, costs associated with the time spent traveling between route sections, or to and from collection boxes, are considered institutional because these activities are incurred irrespective of mail volume and/or mail mix. *Id.* They are not specific to any particular mail product or group of products. *Id.* The volume variabilities for city delivery vehicles are estimated separately for letter routes and SPRs, and the volume-variable costs are distributed based on the mix of products delivered by each route type. *Id.* SPRs are primarily used for parcel and Competitive product delivery, while letter routes are primarily used for delivery of letters and Market Dominant products. *Id.* at 115-16. Consequently, 84 percent of the total attributable costs for vehicle depreciation associated with SPRs were attributed to Competitive products in FY 2020, while 83 percent of the attributable costs for vehicle

¹⁹⁷ *Id.* at 114-15. “Vehicle service drivers” “transport[] mail using postal-owned and leased vehicles[,] . . . generally . . . between post offices, stations, branches, Processing and Distribution Centers/Facilities . . . , Air Mail Centers/Air Mail Facilities . . . , Network Distribution Centers . . . , depots, and certain firm locations[,] . . . [as well as being] stationed at N[etwork] D[istribution] C[enter] facilities.” FY21 Summary Descriptions, file “CS08-21.docx,” at 8-1. “Other vehicles” “are used for administrative purposes.” *Id.* file “CS20-21.docx,” at 20-8.

depreciation associated with letter routes were attributed to Market Dominant products. *Id.* at 116.

Similarly, the depreciation costs associated with vehicle service drivers¹⁹⁸ and rural carriers are volume-variable to the same degree as vehicle service driver labor costs and rural carrier labor costs, respectively. *Id.* In total, 51 percent of the attributable costs for vehicle depreciation were attributed to Market Dominant products in FY 2020, while 49 percent were attributed to Competitive products. *Id.* This is particularly notable considering that Market Dominant products made up 94.48 percent of the Postal Service's total mail volume, whereas Competitive products made up only 5.52 percent. *Id.* The Commission found in Order No. 6043 this demonstrates, contrary to UPS's assertions, that the attribution of vehicle costs does reflect the fact that Competitive products impose costs that are disproportionate to their share of total volume. *Id.*

The institutional portion of vehicle depreciation costs is made up of depreciation costs associated with non-delivery-related administrative vehicles (Cost Component 230, "Other" vehicles), as well as the depreciation costs associated with delivery-related vehicles with respect to activities that do not vary with volume (such as driving from mailbox to mailbox), or simply due to all forms of normal depreciation. *Id.* at 116-17. The Commission found in Order No. 6043 that no portion of vehicle depreciation-related institutional costs is uniquely or disproportionately associated with Competitive products. *Id.* at 117.

The Commission also noted in Order No. 6043 that UPS has previously understated the portion of vehicle depreciation costs being attributed to Competitive

¹⁹⁸ "Vehicle service drivers" "transport[] mail using postal-owned and leased vehicles[,] . . . generally . . . between post offices, stations, branches, Processing and Distribution Centers/Facilities . . . , Air Mail Centers/Air Mail Facilities . . . , Network Distribution Centers . . . , depots, and certain firm locations[,] . . . [as well as being] stationed at N[etwork] D[istribution] C[enter] facilities." FY20 Summary Descriptions, file "CS08-21.docx," at 8-1.

products, individually or as a group. *Id.* Specifically, on appeal UPS asserted that for FY 2018 “only 34.3 [percent] of vehicle depreciation costs . . . [were] attributed to any products—and only 13.96 [percent] to domestic competitive products.”¹⁹⁹ The Cost Segments and Components Report relied upon by UPS illustrates “the volume variable and product specific costs by cost segment and component for domestic Market Dominant products and for domestic Competitive and International products in aggregate.”²⁰⁰ However, product- and group-level inframarginal costs are also attributed to Competitive products, individually and collectively. See Order No. 6043 at Section IV.B.3. In the Cost Segments and Components Report that UPS used for its calculations, inframarginal costs are included in “other” costs.²⁰¹ These costs are shown separately in the summary description report that the Postal Service files annually.²⁰² The actual percentage of vehicle depreciation costs attributable to domestic Competitive products in FY 2018 was 4.2 percentage points higher than alleged by UPS.²⁰³

b. Comments

UPS continues to assert that “[t]he Postal Service[] [is] purchas[ing] . . . costly larger vehicles *designed* to accommodate packages . . .” UPS Comments at 20 (emphasis in original). UPS states that “[t]he high levels of institutional costs associated

¹⁹⁹ UPS Reply Brief at 13 (emphasis omitted) (citing Rule 39 C.F.R. Section 3050.60(f) Report for FY 2018 (Summary Descriptions), July 1, 2019, ZIP file “SummaryDescriptionsFY2018.zip,” folder “CRA.Summary.Description.FY18,” file “CS20-18,” at 20-2 (FY18 Summary Descriptions); Docket No. ACR2018, Library Reference USPS-FY18-2, December 28, 2018, Excel file “FY18Public Cost Segs and Comps.xlsx.” (Cost Segments and Components Report).

²⁰⁰ Library Reference USPS-FY18-2, PDF file “USPS-FY18-2 Preface.pdf.”

²⁰¹ Library Reference USPS-FY18-2, Excel file “FY18Public Cost Segs and Comps.xlsx,” tab “CS20,” cell 59.

²⁰² FY18 Summary Descriptions file “CS20-18,” at 20-1, column “Inframarginal.”

²⁰³ Docket No. ACR2018, Library Reference USPS-FY18-NP10, December 28, 2018, folder “Model,” Excel file “IC2018NP.IC.xlsx,” tab “CS20.” The specific percentage was calculated by Commission staff using data from this file.

with these much larger vehicles designed to carry packages is [a] concrete demonstration of an association between institutional costs and competitive products.” *Id.* at 21. UPS argues that “even if [UPS] [agreed with the methodology used to attribute vehicle costs to individual products], the Commission’s previous responses do not address . . . whether the costs associated with vehicles that are larger than traditional postal vehicles are disproportionately associated with competitive products, and whether the methodology used to calculate the incremental costs of *competitive products as a group* is reliable and accurate.” *Id.* at 22 n.36 (emphasis in original).

With respect to “other vehicles” specifically, UPS states that “the Commission offers no specificity on what . . . ‘administrative purposes’ are, why it is impossible to associate at least some of these costs with competitive products, or why—given the growth of the competitive products business—the Commission cannot conclude that these costs are indeed disproportionately associated with competitive products.” *Id.* at 22 (citing Order No. 6043 at 115 (emphasis omitted)). With respect to city delivery vehicles, “vehicle service drivers,” and vehicles used for rural delivery, UPS argues that the current costing methodology “assumes that there is a direct correlation between the attribution of labor costs and the vehicle costs[] . . . [which] reveals that the Commission is willing to accept imperfect assumptions and estimates when it comes to attributing costs, which highlights the very different standard it applies when it comes to setting the appropriate share.” *Id.* at 22-23 (citing Order No. 6043 at 115).

ASL and its Declarant, Dr. John W. Mayo,²⁰⁴ assert that the reason the Postal Service is acquiring a new fleet of delivery vehicles is because the existing fleet is outdated, lacks modern safety features, and is expensive to maintain—and the need to address these issues exists independent of growth in Competitive product volumes.

²⁰⁴ Dr. Mayo is the Elsa Carlson McDonough Chair of Business Administration and Professor of Economics, Business and Public Policy in Georgetown University’s McDonough School of Business as well as the Executive Director for the Georgetown Center for Business and Public Policy. Mayo Decl. ¶ 1.

ASL Comments at 33-37; Mayo Decl. ¶¶ 31-39. ASL and Dr. Mayo assert that the depreciated costs of the new vehicle fleet will be offset by substantial savings in vehicle maintenance costs compared to the current fleet—savings which Dr. Mayo suggests could be high enough to completely offset the depreciated costs of the new fleet. ASL Comments at 38-41; Mayo Decl. ¶¶ 40-42.

ASL, and its Declarants Dr. Mayo and Dr. Panzar, state that because the new delivery vehicles are capital assets and capital expenses accrue as depreciation, it is not the total cost of the new vehicle fleet that is relevant to the Commission's consideration of costs that are potentially uniquely or disproportionately associated with Competitive products, but rather the annual depreciation cost.²⁰⁵ Moreover, the portion of the annual depreciation cost that is incremental to Competitive products is the difference between the depreciation cost of a vehicle fleet sized to deliver letters, flats, and parcels compared to one that is only sized to deliver letters and flats.²⁰⁶ ASL and Dr. Panzar both maintain that the costs associated with new vehicle purchases are an issue of cost attribution, not an issue relevant to the appropriate share. ASL Comments at 45; Panzar Decl. at 32. These commenters note that under the current costing methodology depreciation costs associated with new vehicles will be attributed to products in the same proportions as the labor costs for the vehicle operators (except for "other vehicles," which are used for administrative purposes and are therefore considered entirely institutional). ASL Comments at 39; Mayo Decl. ¶¶ 43-51. Therefore, over time, if Competitive volumes continue to grow, the distribution keys that distribute attributable costs to products will distribute a larger share of the depreciation costs to Competitive products. ASL Comments at 39; Mayo Decl. ¶¶ 43-51.

²⁰⁵ ASL Comments at 37-38; Mayo Decl. ¶¶ 37-39; Panzar Decl. at 30.

²⁰⁶ ASL Comments at 41; Mayo Decl. ¶ 52; Panzar Decl. at 31.

ASL and Dr. Mayo assert that both cost engineering modeling and vehicle price comparisons show that the incremental cost of additional cargo capacity in new vehicles is a relatively small part of the new vehicles' overall cost. ASL Comments at 41-45; Mayo Decl. at ¶¶ 52-60. Most of the costs associated with new delivery vehicles, according to ASL and Dr. Mayo, are associated with features such as "airbags, anti-lock brakes, air conditioning, back-up cameras, intermittent windshield wipers, blind-spot warning systems, daytime running lights, and seatbelt reminders"—features that have nothing to do with the vehicle's size. ASL Comments at 41-45; Mayo Decl. ¶¶ 52-60. Dr. Mayo estimates that the extra cargo capacity required for parcels on an average city carrier route is 29 cubic feet, which, he asserts, "is only about one quarter of the cargo capacity available on existing (modestly-sized) vehicles in the Postal Service fleet." Mayo Decl. ¶ 54. After reviewing publicly-available information on commercial pricing of cargo vans to determine the relationship between increases in cargo capacity and increases in vehicle cost, Dr. Mayo finds the relationship to be an increase of approximately \$35 for every cubic foot increase in cargo capacity. *Id.* ¶¶ 54-58. Multiplying \$35 by the 29 cubic feet in cargo capacity required for parcels on an average city route, Dr. Mayo finds that "the incremental cost of cargo capacity for an average cube of parcels on a city carrier route equals approximately \$1,015 per vehicle, compared to a base price of approximately \$35,000 to \$40,000." *Id.* ¶ 59. This amount "would correspond to total annual vehicle depreciation costs of approximately \$162 million for Competitive products[] . . ." which, according to Dr. Mayo, "would comprise a minimal share of total attributable costs for Competitive products . . . and is far exceeded by the minimum contribution requirement and the much higher actual Competitive product contribution toward institutional costs." *Id.* ¶ 60.

UPS replies that ASL, Dr. Mayo, and Dr. Panzar's methodology for determining the portion of the new vehicle fleet's costs incremental to Competitive products is flawed because they only consider incremental costs in the short term; they "do[] not consider the long-term, structural changes the Postal Service would make if it did not deliver packages." UPS Reply Comments at 27. UPS states that "[w]ith ever decreasing letter volumes, if the Postal Service were profit-maximizing, it would take the hard steps required to right-size the business and *decrease* the scope and frequency of its delivery network[,]" which "implies the *full amount* of the vehicle investment costs may be considered incremental to packages" *Id.* (emphasis in original). Similarly, "a rational Postal Service offering only market-dominant products (on a steep decline) would purchase a smaller, cheaper, and more streamlined fleet of vehicles to service ever-decreasing volumes of market-dominant products—or maybe not purchase vehicles at all." *Id.* at 28. Therefore, "[t]o measure the incremental costs of the [new vehicle] fleet accurately, the Commission must create a model of the fleet the hypothetical market-dominant Postal Service would purchase and measure the financial difference between the real-world [new vehicle] costs and the hypothetical market-dominant-only fleet costs." *Id.* UPS similarly disputes that the existing costing methodology accounts for Competitive product growth over time, because it "focus[es] only on volume-variable costs[] . . . [,] [which] do not account for the rational restructuring of operations a market-dominant-only Postal Service would undertake in light of collapsing market-dominant volumes." *Id.* at 29-30.

TPA comments that the Postal Service "assumes that network travel . . . cannot be attributed to parcel nor letter deliveries[,]" even though "evidence [suggests] that package deliveries are in fact increasing costs relating to network travel." TPA Reply Comments at 1. Anecdotally, TPA asserts that "tedious package processing has resulted in carrier routes starting later than anticipated[,], [p]ackage delivery complications (e.g., bringing packages to consumers' front doors) can result in additional delays in completing routes[,], [a]nd sufficiently long delays could result in

network travel that coincides with rush hour traffic and/or leads to overtime compensation for [Postal Service] employees.” *Id.* TPA also states that it is “unclear . . . why . . . vehicle depreciation . . . cannot be attributed to competitive nor market dominant products.” TPA Reply Comments, Attachment at 7. TPA suggests that network travel “likely does in fact have a correlation with the mix of mail that the [Postal Service] transports.” *Id.* TPA also states that the Commission’s “characterization of ‘all forms of normal depreciation’ as unattributable institutional costs is . . . dubious[,]” because “[g]ross vehicle weight has a negative relationship with vehicle longevity” *Id.* Finally, TPA asserts that while “[the Postal Service’s] refusal to attribute administrative vehicles is more understandable than some of their other cost attribution policies, . . . at least some of these costs can likely be allocated.” *Id.*

c. Commission Analysis

UPS asserts that the primary purpose of the Postal Service’s new mail delivery vehicles can be inferred solely on the basis of the vehicle’s size, and that, on that basis alone, the costs associated with acquiring the new vehicle fleet that are classified as institutional should be considered uniquely or disproportionately associated with Competitive products. See UPS Comments at 20-22. However, the Commission agrees with ASL, Dr. Mayo, and Dr. Panzar that the issue is, in actuality, much more nuanced than UPS represents.²⁰⁷

As an initial matter, the Commission finds that because delivery vehicles are capital assets and capital expenses accrue as depreciation, it is not the *total* costs of the new vehicle fleet that are relevant to the Commission’s consideration of the degree to which any costs are uniquely or disproportionately associated with Competitive products, but rather the *annual depreciation* costs. Furthermore, the Commission agrees with ASL, Dr. Mayo, and Dr. Panzar that, conceptually, the portion of annual

²⁰⁷ See ASL Comments at 33-39, 41, 41-45; Mayo Decl. ¶¶ 31-60; Panzar Decl. at 30, 31.

depreciation costs associated with new vehicle purchases that is incremental to Competitive products would be the difference between the depreciation cost of a vehicle fleet sized to deliver only Market Dominant products compared to a vehicle fleet sized to deliver both Market Dominant and Competitive products.²⁰⁸ In general, this is a question of cost attribution pursuant to 39 U.S.C. § 3633(a)(1) and (a)(2), unless UPS can show that there are costs related to the acquisition of the new vehicle fleet that are not already being attributed to Competitive products that are nevertheless uniquely or disproportionately associated with Competitive products in an economically sound manner. UPS fails to make such a showing.

UPS argues that unique or disproportionate association with Competitive products can be inferred solely based on the new vehicles being larger than the vehicles that they are replacing. See UPS Comments at 20-22. However, as ASL and Dr. Mayo explain, ample justification exists for a new delivery vehicle fleet completely independent of vehicle size and/or any increase in Competitive product volumes. See ASL Comments at 33-37, 38-41; Mayo Decl. ¶¶ 31-42. Both the U.S. Government Accountability Office and the Postal Service Office of Inspector General acknowledge that the need to replace the Postal Service's current delivery vehicle fleet, which is well

²⁰⁸ See ASL Comments at 41; Mayo Decl. ¶ 52; Panzar Decl. at 31. Practically speaking, the existing costing methodology reaches this result by attributing vehicle depreciation costs to products and groups of products based on the attribution of labor costs for the mail carriers operating the vehicles. See FY 2021 Summary Descriptions file "CS20-21.docx" at 20-1, 20-5 to 20-8. The existing costing methodology accounts for the fact that Competitive products are often larger and heavier, and hence more labor-intensive to process and deliver, than Market Dominant products. Order No. 4963 at 139. Cost drivers include mail characteristics such as weight and shape (e.g., letters or parcels), and costs are distributed to products in proportion to the prevalence of the cost driver within each product. *Id.* Thus, heavier Competitive products have more weight-driven costs attributed to them than lighter products. *Id.* Because the direct cost of carrier labor is substantially greater per piece for Competitive products, and because vehicle depreciation is attributed to products and groups of products based on the direct cost of carrier labor, the amount of vehicle depreciation costs attributed to Competitive products is disproportionately higher than the amount attributed to Market Dominant products.

beyond its intended operational lifespan, requires significant expenditures to maintain and is not up to modern safety and ergonomic standards.²⁰⁹

²⁰⁹ See, e.g., United States Postal Service, Office of Inspector General, Report No. 22-045-R23, Vehicle Maintenance Facility Preparedness for Next Generation Delivery Vehicles, October 17, 2022, at 3 n.4, available at <https://www.uspsoig.gov/sites/default/files/document-library-files/2022/22-045-R23.pdf> (OIG Report No. 22-045-R23) (“As of the end of FY 2021, the Postal Service has approximately 138,000 right-hand-drive LLVs, with an average age of 30 years. All LLVs have exceeded their projected 24-year life span and account for over 63 percent of the delivery fleet.”); United States Postal Service, Office of Inspector General, Report No. RISC-WP-22-003, Electric Delivery Vehicles and the Postal Service, March 17, 2022, at 3, available at <https://www.uspsoig.gov/sites/default/files/document-library-files/2022/RISC-WP-22-003.pdf> (OIG Report No. RISC-WP-22-003) (“For over 35 years, the Postal Service has used Long Life Vehicles (LLVs) as its primary delivery vehicles. LLVs went into service between 1986 and 1994 and were originally designated to have a lifespan of 24 years. Even the youngest LLVs are now far beyond their intended service life and are expensive to operate and maintain.”); United States Postal Service, Office of Inspector General, Report No. DR-MA-14-005, Delivery Vehicle Fleet Replacement, June 10, 2014, at 1, available at <https://www.uspsoig.gov/sites/default/files/dr-ma-14-005-dr.pdf> (OIG Report No. DR-MA-14-005) (“Long-life vehicles (LLV), which comprise 75 percent of the Postal Service’s delivery fleet, have an expected service life of 24 years. The current fleet consists of LLVs that are now between 20 and 27 years old. As the Postal Service’s fleet ages, projected maintenance costs will continue to increase. The Postal Service will increasingly retire older models by necessity due to the high cost of repairing them or the unavailability of replacement parts.”) (footnotes omitted).

Moreover, the Postal Service has elaborated on its need to replace the end-of-life and high-maintenance delivery Long Life Vehicles (LLVs) and Flexible Fuel Vehicles (FFVs) with new vehicles that have more energy-efficient powertrains, updated technology, reduced emissions, increased cargo capacity and improved loading characteristics, improved ergonomics and carrier safety, and reduced maintenance costs. United States Postal Service, Record of Decision and Record of Environmental Consideration, Next Generation Delivery Vehicle Acquisitions, February 23, 2022, App’x A, Final Environmental Impact Statement, Next Generation Delivery Vehicle Acquisitions, December 2021, at i, available at https://uspsngdveis.com/documents/USPS%20NGDV%20Acquisitions%20NEPA%20Record%20of%20Decision_2.23.22.pdf (“Finally, the No-Action Alternative, in addition to having the highest potential environmental impacts of all the alternatives, would not satisfy the Purpose and Need as aged and end-of-life delivery vehicles with outdated safety features and poor performance characteristics would not be replaced leaving the Postal Service unable to fulfill its primary mission to deliver the nation’s mail.”); *id.* App’x B at B-178 (“The [next generation delivery vehicle] acquisition will replace an aging delivery fleet with a purpose built, ergonomic, safer, more fuel efficient and more environmentally friendly vehicle, regardless of the drivetrain selected.”); United States Postal Service, Office of Inspector General, Report No. 19-002-R20, Delivery Vehicle Acquisition Strategy, August 12, 2020, at 5, available at <https://www.uspsoig.gov/sites/default/files/document-library-files/2020/19-002-R20.pdf> (“The backbone of the delivery fleet is the purpose-built [right-hand-drive] LLV, which is used to deliver mail on city and rural routes across the country. The expected service life of these vehicles is 24 years and 69 percent of the current fleet is now between 25 and 32 years old. Over 140,000 delivery and collection vehicles are more than 25 years old. As the fleet continues to age, maintenance costs remain high, and older vehicle models are being retired as they become too costly to maintain or repair.”); OIG Report No. DR-MA-14-

Furthermore, as ASL and Dr. Mayo persuasively demonstrate, the vast majority of the costs associated with acquiring new delivery vehicles have nothing to do with the vehicles' size. See ASL Comments at 41-45; Mayo Decl. ¶¶ 52-60. They are instead associated with the engine and other mechanical and technological components of the vehicles, and such costs would be incurred even if the fleet was sized to deliver only Market Dominant products.²¹⁰

After persuasively establishing the lack of a unique or disproportionate association between the costs associated with acquiring new delivery vehicles and the provision of Competitive products (except for those that are attributed to Competitive products), ASL and Dr. Mayo go further. They demonstrate that even if those costs were found to be uniquely or disproportionately associated with Competitive products (which they are not), the cost of additional cargo capacity for the new vehicle fleet is a relatively small part of the new vehicles' overall cost and is exceeded by the formula-

005 at 9-13 (recommending that the Postal Service consider applicable statutory and regulatory requirements, modern standard safety features that were not available when the LLVs were initially designed and purchased, emerging vehicle technologies and trends, and best practices for fleet management in designing its long-term strategy to replace its aging fleet); United States Government Accountability Office, Testimony Before the Committee on Oversight and Reform, House of Representatives, Fleet Management: Preliminary Observations on Electric Vehicles in the Postal and Federal Fleets, Statement of Jill Naamane, Acting Director, Physical Infrastructure, Report No. GAO-22-105931, April 5, 2022, at 3, available at <https://www.gao.gov/assets/gao-22-105931.pdf> ("Most of the purpose-built vehicles, which USPS purchased from 1987 to 1994, are approaching the end of their useful life. These vehicles do not have modern features such as airbags and air conditioning, and they are experiencing increasing maintenance costs and are at greater risk of safety incidents."); United States Government Accountability Office, Report to Congressional Requesters, United States Postal Service: Strategy Needed to Address Aging Delivery Fleet, Report No. GAO-11-386, May 5, 2011, available at <https://www.gao.gov/assets/gao-11-386.pdf> (recommending that the Postal Service develop a strategy for addressing its aging delivery fleet needs that considers the effects of likely operational changes, legislative fleet requirements, and other factors).

²¹⁰ OIG Report No. 22-045-R23 at 3 ("Furthermore, the [next generation delivery vehicle] will be equipped with many new features representing significant technical advancements when compared to the LLV – air conditioning, 360-degree cameras, advanced braking and traction control, air bags, and collision avoidance systems"); OIG Report No. RISC-WP-22-003 at 1 ("The upfront cost of buying a new electric delivery vehicle is significantly higher than the cost of buying a new gasoline-powered vehicle. Electric vehicles also require the installation of chargers and related electrical infrastructure, which further adds to the upfront costs. Once the vehicle is purchased and the charger installed, electric vehicles are generally cheaper to operate because energy and maintenance costs are lower.").

based appropriate share alone (and by actual Competitive product contribution to institutional costs). See ASL Comments at 44-45; Mayo Decl. ¶¶ 38-39.

Moreover, the existing cost attribution methodology distributes vehicle depreciation costs to products in the same proportion as the labor costs of the mail carriers operating the vehicles. As a result, the disproportionately higher labor costs associated with processing and delivering Competitive products translate into vehicle depreciation costs being disproportionately attributed to Competitive products—and this amount will only increase if Competitive product volumes continue to increase. UPS questions the assumption that labor costs are correlated with vehicle costs, but that assumption is logical because the purpose of mail delivery vehicles is to support mail delivery, and hence carriers' delivery activities constitute a fair reflection of the uses to which the vehicles are being put.

UPS criticizes the existing costing methodology as well as ASL and Dr. Mayo's estimate of the incremental cost of extra cargo capacity on new delivery vehicles for not taking into account the amount by which costs could be reduced in the long run through a rational restructuring of the scope and frequency of the Postal Service's operations if the Postal Service did not deliver Competitive products. See UPS Reply Comments at 27-29. However, as explained *supra* at Section IV.C.2., this argument ignores that legal obligations limit the Postal Service's ability to undertake the type of hypothetical restructuring that the long-term incremental costing UPS speculates about would be premised upon, such as reducing the scope or frequency of the Postal Service's network. These legal requirements would remain even if the Postal Service did not deliver any Competitive products, and have no bearing on the extent to which costs are incremental to Competitive products. Moreover, as explained *infra* at Section VIII.C.3., UPS's proposed approach to the development of long-run incremental costs suffers from numerous flaws and is inconsistent with the PAEA. UPS's calculations of long-run incremental costs rely upon a hypothetically efficient Market Dominant enterprise that

does not exist and, as a result, would capture not only costs that are uniquely or disproportionately associated with Competitive products but also costs that occur due to inefficiencies in the network with respect to Market Dominant products.²¹¹

UPS also questions the accuracy of the existing costing methodology with respect to the calculation of group-level incremental costs for Competitive products (UPS Comments at 22 n.36), but UPS does not specify what part of the existing costing methodology it finds problematic, other than that it “does not account for costs uniquely or disproportionately associated with competitive products more broadly.” *Id.* at 22. The Commission explained the existing costing methodology in detail in Order No. 6043, and UPS does not show that the application of that methodology to vehicle depreciation costs is in any way inaccurate. Moreover, as explained above, UPS has not demonstrated that any costs beyond those which are already being attributed to Competitive products at the product or group level through the existing costing methodology are uniquely or disproportionately associated with Competitive products.

TPA asserts that “evidence [suggests] that package deliveries are . . . increasing costs relating to network travel[,]” but the “evidence” on which TPA purports to rely (“tedious package processing . . . result[ing] in carrier routes starting later than anticipated[,]” “[p]ackage delivery complications . . . result[ing] in additional delays in completing routes[,]” and “delays . . . result[ing] in network travel that coincides with rush hour traffic and/or leads to overtime compensation for USPS employees”) is all anecdotal. See TPA Reply Comments at 1. Similarly, TPA, mentioning recent increases in overtime labor costs by the Postal Service, contends that “[b]ecause vehicle depreciation costs are attributed in the same proportions as the labor costs for the carriers operating the vehicles . . . there is likely some relationship between overtime-driven network travel costs and increased package volume.” *Id.* Attachment at

²¹¹ See Panzar Reply Decl. at 12-14; UPS Comments at 51. See also Section VIII.C.3., *infra*.

7 (internal marks omitted). There is no indication of the extent to which such circumstances are actually occurring, the extent to which such circumstances are meaningfully related to increased package volume (beyond those costs for which the Commission already classifies under 39 U.S.C. § 3633(a)(1) and (a)(2) and therefore already form the mathematical base of the 39 U.S.C. § 3633(a)(3) price floor), and hence to what extent they might be affecting institutional costs (if they do at all). Moreover, as the Commission has previously noted “[g]enerally, compensation cost for additional overtime is lower than for additional straight time because benefit costs do not increase with overtime workhours.” FY 2021 Financial Report at 106. TPA’s assertion of a relationship between overtime costs and package volume does not reflect the use of overtime by the Postal Service as a cost management strategy. As a result, TPA’s assertions are purely speculative and thus lack a reasonable basis to justify altering the Commission’s formula-based approach.

With respect to “other vehicles” used for administrative purposes, UPS and TPA question why it is impossible to associate at least some of the vehicle depreciation costs with Competitive products, “or why—given the growth of the competitive products business—the Commission cannot conclude that these costs are indeed disproportionately associated with competitive products.” UPS Comments at 22; TPA Reply Comments, Attachment at 7, 8. TPA similarly questions why network travel cannot be attributed, given that “the time spent traveling between route sections . . . likely does in fact have a correlation with the mix of mail that the USPS transports,” since transporting and distributing packages takes clerks “much longer than sorting letters . . . [.]” and “[i]f the clerks are delayed, the station’s carriers will be delayed in starting routes, which are already longer than ever thanks to . . . packages” TPA Reply Comments, Attachment at 7 (internal marks omitted). TPA also questions why “normal depreciation” cannot be attributed to vehicles, given that “[g]ross vehicle weight has a negative relationship with vehicle longevity” *Id.*

As the Commission has explained, “other vehicles” are not used for mail transportation or delivery, and thus there is no basis for attributing them to any products or groups of products. Order No. 6043 at 115. Moreover, the total amount of costs in this component—\$19.2 million in FY 2020—is very small relative to the Postal Service’s total vehicle depreciation costs and is dwarfed by the formula-based appropriate share (as well as by the actual Competitive product contribution to institutional costs). The same is true for network travel and normal depreciation—these are costs that would be incurred regardless of mail volume and/or mail mix, and thus there is no basis to attribute them to any specific product or group of products. *Id.* at 115, 116-17. Network travel is the time spent on a mail route traveling between delivery sections, or to and from collection boxes, and as such it is unclear how it would be affected by delays starting the route.²¹² Furthermore, even if gross vehicle weight is negatively correlated with vehicle longevity, that would have no effect on the rate of depreciation over the relevant depreciation timeframe, which is determined at the time of acquisition based on the expected life of the vehicle. In any event, depreciation costs, as well as maintenance costs, are attributed to products on the basis of the labor of the carriers using the vehicles. Because Competitive products take proportionally longer for carriers to deliver, any increase in the volume of Competitive products will also disproportionately increase the vehicle depreciation and maintenance costs attributed to Competitive products. Overall, the commenters’ conjecture and dissatisfaction with the results of the economically sound methodologies applied by the Commission fail to meaningfully rebut

²¹² See FY21 Summary Descriptions, file “CS07-21.docx,” at 7-3. While the time spent servicing mailboxes on a mail route is attributed to products and groups of products based on the proportions of products being picked up or delivered, network travel is a function of the delivery network. See *id.* Such activities are incurred by the Postal Service irrespective of mail volume and/or mail mix. *Id.* As such, network travel is not uniquely or disproportionately associated with any specific products or groups of products.

TPA (or any interested person) is welcome to file a petition in the future to initiate a rulemaking proceeding if TPA believes that it can demonstrate a causal link between network travel and any specific products or groups of products on which attribution could be based. See 39 C.F.R. § 3050.11(a).

the Commission's explanation appearing in Order No. 6043. See Order No. 6043 at 114-17. The Commission has considered the depreciation costs associated with new vehicle purchases and finds that, except for those that are attributed to Competitive products, they are not uniquely or disproportionately associated with Competitive products. Furthermore, even if they were (which they are not), UPS has failed to offer a reasoned basis to alter the Commission's formula-based approach to account for these costs, which are significantly less than the formula-based appropriate share (and are significantly less than actual Competitive product contribution to institutional costs).²¹³

2. City Carrier Assistant Costs

a. Prior Commission Findings

In response to allegations by UPS that growth in the number of Postal Service employees, including city carrier assistants, suggested that growth in package volume was placing a disproportionate demand on the Postal Service's delivery network, the Commission explained that the Postal Service hires new city carriers or city carrier assistants for numerous reasons that are unrelated to Competitive product volumes. Order No. 6043 at 118. For example, an increase in delivery points can result in additional routes, increasing the need for additional carriers even when Market Dominant and Competitive volumes remain unchanged.²¹⁴ A simple analysis of volume trends cannot establish a meaningful relationship between costs and any particular product or group of products. Order No. 6043 at 118. Instead, a sophisticated

²¹³ The institutional costs associated with vehicle depreciation in FY 2021 totaled \$131.3 million. See FY21 Summary Descriptions, file "CS20-21.docx," at 20-1. This is well below either the formula-based appropriate share for FY 2021 (9.1 percent of institutional costs, or \$3.061 billion) or actual Competitive product contribution to institutional costs in FY 2021 (39.2 percent of institutional costs, or \$13.193 billion). See FY 2021 ACD at 96; Docket No. ACR2021, United States Postal Service FY 2021 Annual Compliance Report, December 29, 2021, at 88-89 (FY 2021 ACR).

²¹⁴ *Id.* at 118 n.186 (citing Order No. 5763 at 87 (noting 10 percent increase in the number of delivery points from FY 2007 to FY 2019)).

methodology is applied to identify the cost of city carrier labor (including city carrier assistants) that is caused by the provision of each product and group of products. *Id.*

Under the current costing methodology, costs associated with city carriers are divided into two cost segments: Cost Segment 6 for in-office activities and Cost Segment 7 for delivery activities.²¹⁵ In-office activities primarily involve preparing mail for delivery before leaving the office for street work. FY21 Summary Descriptions, file “CS06-21.docx,” at 6-1. In-office activities also include maintaining operational records and performing administrative duties. *Id.* Order No. 6043 observed that in FY 2020, approximately 88 percent of the Cost Segment 6 costs were attributed, with 26 percent of those costs attributed to Competitive products collectively.²¹⁶ This is notable given that Competitive products made up only 5.52 percent of total mail volume in FY 2020.²¹⁷

Cost Segment 7 covers all the “salaries, benefits, and related costs of street activities for letter routes . . . ,” as well as “city carriers performing activities for special purpose routes including both in-office and street activities combined.” FY21 Summary Descriptions, file “CS07-21.docx,” at 7-1. City carrier street activity costs within Cost Segment 7 are developed in two separate groups—letter routes, and SPRs. *Id.* Letter routes encompass more than 90 percent of accrued street costs, with SPRs used to deliver parcels and collect mail from dense urban areas. *Id.* Letter route delivery activity includes “traveling between customer stops within delivery sections; preparing mail to be delivered on the route; accessing and loading customer receptacles; deviations for large parcels and accountables; and collecting outgoing mail from

²¹⁵ FY21 Summary Descriptions, file “CS06-21.docx,” at 6-1; FY21 Summary Descriptions, file “CS07-21.docx,” at 7-3.

²¹⁶ Order No. 6043 at 119 (citing Docket No. ACR2020, Library Reference USPS-FY20-NP10, December 29, 2020, folder “Model,” Excel file “IC2020NP.IC.xlsx,” tab “CS06”). The specific percentages were calculated by Commission staff using the data from this worksheet.

²¹⁷ Order No. 6043 at 119 (citing Docket No. ACR2020, Library Reference PRC-LR-ACR2020-1, March 29, 2021, folder “PRC-LR-ACR2020-1.zip,” Excel file “FY20 Summary_LR-1.xlsx”). The specific percentages were calculated by Commission staff using the data from this file.

customers and designated collection points (e.g., collection boxes).” *Id.* at 7-3. SPR delivery activity includes “the in-office portion of sequencing and loading parcels, parcel and bulk deliveries, Sunday delivery, extra peak season delivery, and collecting mail at designated collection points.” *Id.* at 7-4.

For letter routes and SPRs, the Postal Service separately estimates a series of econometric equations to compute variabilities and develop distribution keys for each cost pool.²¹⁸ For further refinement of SPR costs, the Postal Service estimates separate variability equations for peak and non-peak periods. FY21 Summary Descriptions, file “CS07-21.docx,” at 7-4. Order No. 6043 observed that in FY 2020 approximately 46 percent of Cost Segment 7 costs for city carriers were attributed, with 26 percent of those costs attributed to Competitive products collectively.²¹⁹ Again, this is notable given that Competitive products made up only 5.52 percent of total mail volume in FY 2020.²²⁰

City carrier costs associated with the time spent traveling between route sections, or to and from collection boxes, are considered institutional because those activities are incurred by the Postal Service irrespective of mail volume and/or mail mix. FY21 Summary Descriptions, file “CS07-21.docx,” at 7-3. Such costs are a function of the delivery network; they are not uniquely or disproportionately associated with Competitive products. Order No. 6043 at 120.

²¹⁸ *Id.* at 7-2-7-5. In Docket No. RM2019-6, the Commission approved a request by the Postal Service to update cost attribution procedures for SPRs based on a new cost study of SPRs that uses operational carrier data to reflect the current structure of SPR activities. See Docket No. RM2019-6, Order on Analytical Principles Used in Periodic Reporting (Proposal One), January 14, 2020, at 1-2, 41 (Order No. 5405).

²¹⁹ Order No. 6043 at 120 (citing Docket No. ACR2020, Library Reference USPS-FY20-NP10, folder “Model,” Excel file “IC2020NP.IC.xlsx,” tab “CS07”). The specific percentages were calculated by Commission staff using the data from this worksheet.

²²⁰ Order No. 6043 at 120 (citing Library Reference PRC-LR-ACR2020-1, folder “PRC-LR-ACR2020-1,” Excel file “FY20 Summary_LR-1.xlsx”). The specific percentages were calculated by Commission staff using the data from this file.

b. Comments

In response to Order No. 6043, UPS asserts that “[the Commission’s] explanation fails to address the critical point: Market-dominant volumes have been plummeting for over a decade, while competitive volumes have surged.” UPS Comments at 23. Thus, according to UPS, “it is logical to conclude that, even if new delivery points have been added, the hiring of tens of thousands of *additional* city carrier assistants and other employees is disproportionately associated with competitive products, and the Commission should consider these costs when setting the appropriate share.” *Id.* (emphasis in original).

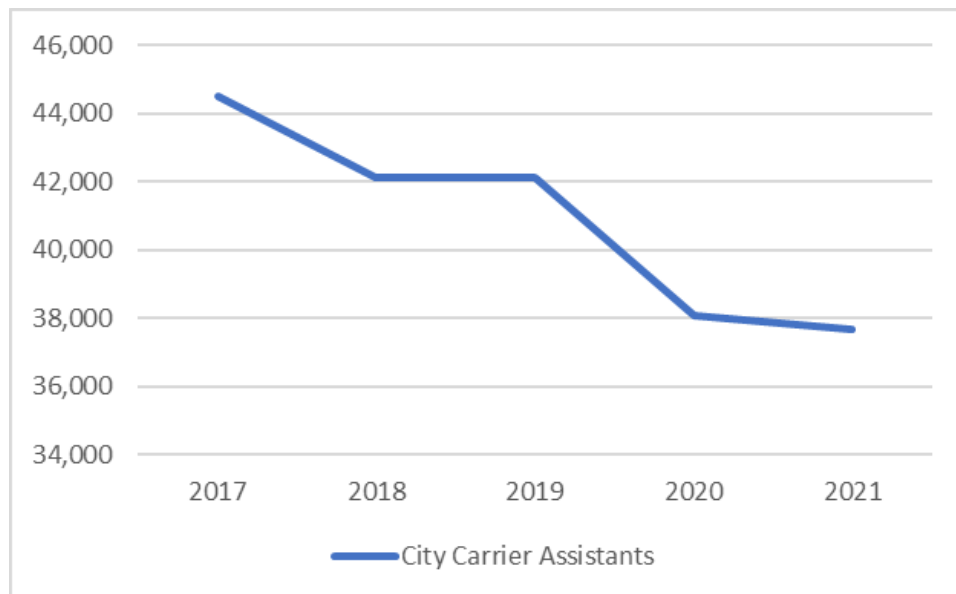
c. Commission Analysis

UPS does not seriously engage with the Commission’s detailed findings appearing in Order No. 6043. See Order No. 6043 at 118-20. UPS continues to speculate that because increases in Competitive product volumes have coincided with the hiring of additional city carrier assistants by the Postal Service, the increases in Competitive product volumes must be either the cause of, or uniquely or disproportionately associated with, the increase in city carrier assistants. As the Commission explained in Order No. 6043, a simple analysis of volume trends is insufficiently persuasive to establish the degree to which a unique or disproportionate association may exist between costs and specific products (or groups of products). The existing costing methodology employs a sophisticated analysis grounded in sound economics to identify and distribute the costs related to city carrier assistants based on the work actually being performed by city carrier assistants. UPS does not specify what aspect of that methodology it finds problematic other than its result.

The growth in the number of city carrier assistants has to some extent been strategic on the Postal Service’s part, as the hourly wages for these non-career employees are less than would be required for career employees that receive full

benefits. See FY 2021 Financial Report at 99. Moreover, this trend has been declining since UPS first raised this issue in 2017,²²¹ as depicted in Figure VII-1 below.

Figure VII-1
Total Number of City Carrier Assistants,
FY 2017–FY 2021



Source: Docket No. ACR2021, Library Reference USPS-FY21-17, December 29, 2021, PDF file “FY 2021 Annual Report to Congress.pdf,” at 29; Docket No. ACR2020, Library Reference USPS-FY20-17, December 29, 2020, PDF file “FY2020 Annual Report.USPS.FY20.17.Rev.5.14.2021.pdf,” at 28; Docket No. ACR2019, Library Reference USPS-FY19-17, December 27, 2019, PDF file “Download FY19.Annual.Report.USPS.FY19.17.pdf,” at 16; Docket No. ACR2018, Library Reference USPS-FY18-17, December 28, 2018, PDF file “Download USPS.FY18.17_Annual Report to Congress.pdf,” at 13; Docket No. ACR2017, Library Reference USPS-FY17-17, December 29, 2017, PDF file “Download USPS.FY17.17.Annual Report.pdf,” at 11.

²²¹ “From 2013 to 2016 the Postal Service on net hired over 20,000 new employees[,]” and “[h]alf of this increase consisted of new hires in the category of ‘City Carrier Assistant’” UPS Order No. 3624 Comments at 31-32.

Figure VII-1 shows that since UPS first made allegations concerning the growth in city carrier assistants in 2017, the number of city carrier assistants has actually been declining, even as Competitive product volume has grown. This undermines UPS's argument that the number of city carrier assistants is correlated with Competitive product volume. It is furthermore not clear from UPS's comments the extent to which UPS has considered employee turnover when referring to the Postal Service's overall number of new hires for city carrier assistants. The Postal Service has long had significant turnover problems with respect to its non-career workforce, especially for city carrier assistants, as detailed in a report from the Postal Service Office of Inspector General issued only a few months before UPS filed its 2017 comments.²²² To the extent that the hiring of additional city carrier assistants has been at least partly in response to growth in Competitive product volumes, it should be noted that the cost of city carrier assistants are included in Cost Segments 6 and 7, and the attribution of those costs to Competitive products has also increased.²²³ The Commission has considered the costs associated with city carrier assistants and finds that, except for those that are attributed to Competitive products, they are not uniquely or disproportionately associated with Competitive products.

²²² See United States Postal Service, Office of Inspector General, Report No. HR-AR-17-002, Non-Career Employee Turnover, December 20, 2016, available at <https://www.uspsoig.gov/sites/default/files/document-library-files/2016/HR-AR-17-002.pdf>. Additionally, the Postal Service Office of Inspector General conducted an audit of Postal Service non-career employee turnover for FY 2016 through FY 2018 nationwide. See United States Postal Service, Office of Inspector General, Report No. 19POG001SAT000-R20, Effectiveness of the Postal Service's Efforts to Reduce Non-Career Employee Turnover, February 12, 2020, at 10, available at <https://www.uspsoig.gov/sites/default/files/document-library-files/2020/19POG001SAT000-R20.pdf>.

²²³ Between FY 2013 and FY 2016, volume-variable and product-specific costs in Cost Segment 6 attributed to Competitive products increased 38.8 percent, and volume-variable and product-specific costs in Cost Segment 7 attributed to Competitive products increased 37.1 percent. Compare Docket No. ACR2013, Library Reference USPS-FY13-2, December 27, 2013, Excel file "FY13.Public CS&CRpt.Revised.xls," tabs "CS06" and "CS07," with Docket No. ACR2016, Library Reference USPS-FY16-2, December 29, 2016, Excel file "FY16Public Cost Segs and Comps.xls," tabs "CS06" and "CS07."

3. Headquarters and Management Costs

a. Prior Commission Findings

In response to allegations by UPS that many of the costs associated with the Postal Service's headquarters and management are necessarily associated with Competitive products, despite being treated as mostly institutional under the current costing methodology, the Commission in Order No. 6043 explained that the specific costs cited by UPS cover a wide variety of employment categories and are not specific to just postal management.²²⁴ Headquarters costs (Cost Component 191) consist of personnel costs of administration and management of operations. FY21 Summary Descriptions, file "CS18-21.docx," at 18-5. As such, they do not fluctuate with changes in mail volume. *Id.* Further, the work covered by this cost component is generally not specific to any particular mail product or group of products. Order No. 6043 at 122.

However, the Postal Service assigns a portion of its headquarters costs to domestic Competitive products in accordance with procedures approved by the Commission in Docket No. RM2008-2 for identifying and applying group-specific costs within Cost Segment 18.²²⁵ Under these procedures, the Postal Service analyzes the various headquarters offices within Cost Segment 18 to determine if that office's activity only, or primarily, supports either Market Dominant products or Competitive products. Order No. 6043 at 122 (citing Order No. 115 at 11). The Postal Service is authorized to categorize an activity as group-specific if it unambiguously supports one product group

²²⁴ Order No. 6043 at 122. The specific costs cited by UPS are in Cost Segment 18, Component 191 ("Headquarters Product Specific"). *Id.* Cost Component 191 contains "administration personnel costs reflect[ing] the costs of managing ongoing postal operations[,...]includ[ing] the personnel costs of Headquarters facilities, the Postal Regulatory Commission, Office of Inspector General, Law Offices, Stamp Distribution Network, Accounting Service Centers, Rates and Classification Service Centers, Human Resource Service Centers, Communications offices, and the Information Service Centers." *Id.* (citing FY20 Summary Descriptions, file "CS18-20.docx," at 18-5).

²²⁵ *Id.* See Docket No. RM2008-2, Order Accepting Certain Analytical Principles for Use in the Postal Service's Periodic Reports, October 10, 2008, at 4-13 (Order No. 115).

(i.e., either Market Dominant products or Competitive products). Order No. 6043 at 122-23 (citing Order No. 115 at 11). In FY 2021, the Postal Service attributed \$29.465 million in product- and group-specific costs from Cost Component 191. FY21 Summary Descriptions, file “CS18-21.docx,” at 18-2. The group-specific portion was attributed to domestic Competitive products collectively, while the remainder—the product specific-portion—was attributed to Address Management Services and international products. *Id.* at 18-5.

UPS also raised similar arguments for other specific cost categories such as “Inspection Service Field Support,” “Data Processing Supplies and Services,” and “Building Projects Expenses.” Order No. 6043 at 121. As the Commission explained in Order No. 6043, however, none of these costs identified by UPS can be identified as uniquely or disproportionately associated with Competitive products. *Id.* at 123-25. To the extent that these costs are classified as institutional, it is because the activities or assets for which they are incurred are not specific to any mail product or group of products, and they would be incurred even if the Postal Service did not deliver any Competitive products. *Id.*

For “Data Processing Supplies and Services,” in particular, the Commission noted that the specific “Data Processing Supplies and Services” costs raised by UPS are in Cost Segment 16, Component 174 (“[Automated Data Processing (ADP)] Supplies and Services Product Specific”). *Id.* at 124. Cost Component 174 contains “costs...for repair and maintenance of ADP equipment; ADP programming; software preparation; contracted ADP services and telecommunications equipment[,] [as well as]...product specific costs for the provision of the Address Management System and international products.”²²⁶ As indicated by the description, the majority of the costs covered by this component are not specific to any particular mail product or group of

²²⁶ *Id.* (quoting FY20 Summary Descriptions, file “CS-16-20.docx,” at 16-7); *accord* FY21 Summary Descriptions, file “CS-16-21.docx,” at 16-7.

products. Order No. 6043 at 124. These costs do not vary with volume and a majority of them are therefore treated as institutional. *Id.* There is a portion, however, which is considered product-specific to the provision of the Address Management System (AMS)²²⁷ and international products, and it is therefore attributed.²²⁸

b. Comments

In response to Order No. 6043, UPS argues that the Commission's "assertion[s] [are] unconvincing[.]" because "[i]f the Postal Service did not deliver any competitive products, it would obviously be able to 'reduce certain headquarters expenses relating to administration and management'" UPS Comments at 24 (citation omitted). Furthermore, "[t]he Postal Service also would be able to decrease expenses for data processing supplies and services." *Id.* at 24-25. UPS argues that "[t]he Commission has failed to substantively address [its] . . . arguments about how institutional costs include those that are incremental to competitive products[,] [but] [i]nstead . . . merely cites the existing, antiquated cost methodology, . . . making no further effort to determine the proportion or amount of institutional costs the Postal Service could eliminate under an efficient reorganization if it did not deliver competitive products." *Id.* at 25. TPA similarly comments that "little or no headquarter expenses [are assigned] to packages or letters, despite headquarter labor expenses going toward analyzing specific lines of postal business and negotiating deals involving discounted, bulk package deliveries." TPA Reply Comments at 1; *id.* Attachment at 9.

²²⁷ The AMS is the Postal Service master database of deliverable addresses. See United States Postal Service, Publication 32 - Glossary of Postal Terms, available at https://about.usps.com/publications/pub32/pub32_terms.htm. Address Management Services is a Market Dominant product. See MCS § 1515.

²²⁸ Order No. 6043 at 124 (citing FY20 Summary Descriptions, file "CS-16-20.docx," at 16-7); *accord* FY21 Summary Descriptions, file "CS-16-21.docx," at 16-7-16-8.

c. Commission Analysis

UPS's criticism of the existing costing methodology with respect to headquarters and management costs is that the costing methodology should be based on long-run incremental costs. However, as explained *infra* at Section VIII.C.3., UPS's proposed approach to the development of long-run incremental costs suffers from numerous flaws and is inconsistent with the PAEA. Moreover, as further discussed *infra* at Section VIII.C.3., the claim that any potential savings in management costs associated with an "efficient reorganization" are costs that must be uniquely or disproportionately associated with Competitive products includes an implicit assumption that any inefficiencies in the Postal Service's management costs are uniquely or disproportionately associated with Competitive products. However, there is no reason to assume that any existing inefficiencies in management costs are uniquely or disproportionately associated with Competitive, but not with Market Dominant, products. See TPA Reply Comments at 1; *id.* Attachment at 9. Beyond its criticism of the cost attribution process, UPS has not offered any reason why these costs should be considered uniquely or disproportionately associated with Competitive products other than speculation that Competitive products "are the subject of greater attention by Postal Service management[.]" UPS Order No. 3624 Comments at 4.

Overall, the commenters' conjecture and dissatisfaction with the results of the economically sound methodologies applied by the Commission fail to meaningfully rebut the Commission's explanation appearing in Order No. 6043. See Order No. 6043 at 122-25. The Commission has considered the costs associated with headquarters and management and finds that, except for those that are attributed to Competitive products,²²⁹ they are not uniquely or disproportionately associated with Competitive products.

²²⁹ See, e.g., Docket No. ACR2020, Library Reference USPS-FY20-NP10, Excel file "FY 2020 Competitive Product Group Specific HQ Costs.xlsx."

4. Supply Personnel and City Carrier Street Time

a. Prior Commission Findings

In response to criticism from UPS regarding the Commission's calculation of volume variability for certain cost components, including supply personnel and city carrier street time, on the grounds that it is based on "judgment" or on econometric studies, the Commission in Order No. 6043 explained that estimating variabilities using econometric studies, or even judgment, is a well-known economic practice. Order No. 6043 at 126. For some smaller components for which data are not sufficient to conduct a quantitative study, Postal Service analysts employ expert judgment to assess their variability. *Id.* Whatever the source, these variabilities indicate how costs would change in response to changes in volume. *Id.* at 126-27. To obtain volume-variable costs for a cost component, the accrued costs for that component are multiplied by the respective volume variability. *Id.* at 127.

As the Commission explained, any costing methodology employs some assumptions and therefore includes some judgment. *Id.* For example, an econometric analysis might contain judgments concerning the following: what panel of facilities or times to use for sampling the data; how to collect data; what functional form to use in the model; and what variables to include. *Id.* The Commission also noted that UPS's argument with respect to these costs substantially echoes the relief it requested in UPS Proposal Two, which was rejected by the Commission in Docket No. RM2016-2. *Id.* (citing Final Order No. 3506 at 62-65, 84-109). There are some cost pools (mostly with relatively few dollars in them, certainly not enough to substantively change the cost coverage of Competitive products collectively) where the variability is based on reasoned judgment and not an empirical or explicit theoretical model. Order No. 6043 at 127. UPS demonstrated that some of those cost pools with zero variabilities exhibited some correlation with volume. *Id.* Of course, correlation does not imply causation, and upon examination of the costs in these pools and the activities that drive

them, most did not have an obvious logical basis for how they would respond to changes in volume in a meaningful way. *Id.* The Commission did, nevertheless, instruct the Postal Service to look at them again (many had not been modified in some time) to make sure there is a reasonable basis for the methodology. *Id.* The Commission found in Order No. 6043 that UPS had not presented a theory regarding what the alleged relationship of these costs is to Competitive products other than causation (which would be an issue for a rulemaking proceeding to consider a methodology for potentially attributing them). *Id.*

The specific “Supply Personnel” costs UPS cites are in Cost Segment 16, Component 173. *Id.* These employees select, pack, ship, and inventory supplies that do not vary with mail volume. Hence, as is evident from this component’s description, it does not contain any volume-variable costs: “[s]upply personnel are stationed at the Supply Center in Topeka, Kansas. The supply center maintains and distributes supplies, forms, and equipment to smaller post offices.” *Id.* at 127-28 (quoting FY20 Summary Descriptions, file “CS16-20.docx,” at 16-4).

With respect to city carrier street time, as previously discussed, volume variabilities for city carrier labor within Cost Segment 7 are estimated by the Postal Service using a series of econometric equations. Order No. 6043 at 128 (citing FY20 Summary Descriptions, file “CS07-20.docx,” at 7-4-7-5). For SPRs, the Postal Service estimates separate variability equations for peak- and non-peak periods. Order No. 6043 at 128 (citing FY20 Summary Descriptions, file “CS07-20.docx,” at 7-4). The Postal Service does make some assumptions in its attribution of Cost Segment 7 costs. Order No. 6043 at 128 (citing FY20 Summary Descriptions, file “CS07-20.docx,” at 7-2). However, the Commission found in Order No. 6043 that those assumptions are reasonable as they are founded in facts, observations, and logic. Order No. 6043 at 128. For example, the Postal Service assumes that network travel is institutional based on the fact that network travel is a function of the delivery network and not related to

changes in volume. *Id.* (citing FY20 Summary Descriptions, file “CS07-20.docx,” at 7-3). The Postal Service also assumes that costs for Cost Component 50 (“Delivery Activities Support”) vary to the same degree as costs for letter route delivery activities, and that costs for Cost Component 53 (“Network Travel Support”) vary to the same degree as costs for letter route network travel. Order No. 6043 at 128 (citing FY20 Summary Descriptions, file “CS07-20.docx,” at 7-6-7-7). These assumptions allow the Postal Service to attribute support activity costs, even though the relationship between support activities and specific products or group of products is not direct. Order No. 6043 at 128. The Commission noted that if UPS disputes a specific assumption, it can petition the Commission to consider an alternate assumption or an alternate costing methodology for these costs. *Id.*

b. Comments

In response to Order No. 6043, UPS asserts that “[its] point was not that econometric judgment is always inappropriate, but that such judgment appears to have resulted in under-attribution of costs to products[,]” which “further highlights that costs associated with competitive products are being classified as institutional.” UPS Comments at 26.

c. Commission Analysis

UPS does not seriously engage with the Commission’s detailed findings appearing in Order No. 6043 and instead repeats its dissatisfaction with the results of the economically sound methodologies applied by the Commission. See Order No. 6043 at 126-28. UPS continues to assert that costs for supply personnel and city carrier street time are being under-attributed to Competitive products, but to the extent UPS believes the existing costing methodology is inaccurate, that is beyond the scope of the instant proceeding. The proper avenue for addressing such a concern would be for UPS to petition the Commission to initiate a proceeding to consider a proposal to

change an accepted analytical principle pursuant to 39 C.F.R. § 3050.11(a).²³⁰ UPS alleges that costs “associated” with Competitive products are being classified as institutional, but UPS does not allege that any such costs are uniquely or disproportionately associated with Competitive products in an economically sound manner, nor does UPS make any showing that would be sufficient to support such a claim. The Commission has considered the costs associated with supply personnel and city carrier street time and finds that, except for those that are attributed to Competitive products, they are not uniquely or disproportionately associated with Competitive products.

5. Package Processing and Delivery Technology

a. Prior Commission Findings

In response to allegations by UPS that many costs pertaining to package processing and delivery technology are uniquely or disproportionately associated with Competitive products, the Commission in Order No. 6043 explained that capital equipment purchased by the Postal Service is recorded as a balance sheet asset, the cost of which is recorded over the asset’s useful life as depreciation. Order No. 6043 at 129. Depreciation costs are distributed to products within cost pools, with each cost pool having its own variability and distribution keys. *Id.*

By way of example, the Commission noted that the depreciation costs of Passive Adaptive Scanning System (PASS) and Delivery Scanning System (DSS) units had a

²³⁰ Any interested party may petition the Commission to initiate proceedings to consider proposals to change an accepted analytical principle. 39 C.F.R. § 3050.11(a). The Commission may also initiate a proceeding to change an accepted methodological principal *sua sponte*. *Id.* These proceedings, which are filed in rulemaking dockets, are intended to improve the quality, accuracy, or completeness of data or data analysis in the reports the Postal Service submits each year to the Commission. *Id.* The Commission has long encouraged interested parties to bring such issues to the Commission’s attention, and a rulemaking docket is the appropriate forum for the types of allegations that UPS makes in this docket with respect to the Commission’s costing methodologies.

variability of 97.4 percent in FY 2020, and were distributed to products based on Revenue, Pieces, and Weight parcel volumes.²³¹ Volume-variable depreciation costs for retail and processing equipment such as Point of Service (POS ONE) units and Intelligent Mail Device (IMD) and Mobile Delivery Device (MDD) scanners are considered to be as volume-variable as the labor costs of the personnel that operate the equipment.²³² Those volume-variable costs are distributed to products in the same proportion as labor costs. Order No. 6043 at 129 (citing FY20 Summary Descriptions, file “CS20-20.docx,” at 20-4). POS ONE units had a 38.5 percent variability in FY 2020. Order No. 6043 at 129 (citing FY20 Summary Descriptions, App’x F at F-2). IMD scanners had a 51.8 percent variability. Order No. 6043 at 129 (citing FY20 Summary Descriptions, App’x F at F-2). MDD scanners had a 45.2 percent variability. Order No. 6043 at 129 (citing FY20 Summary Descriptions, App’x F at F-2). Each of these equipment categories uses the same distribution as the labor costs of the equipment operator. Order No. 6043 at 129 (citing FY20 Summary Descriptions, App’x F at F-2). As a result, the portion of these costs that is associated with Competitive products is attributed to them. Order No. 6043 at 129.

b. Comments

In response to Order No. 6043, UPS asserts that “the Commission fails to acknowledge that [its] depreciation methodology inevitably results in costs associated with competitive products being classified as institutional.” UPS Comments at 27. UPS maintains that “[p]lainly a significant portion (if not all) of the[] institutional costs [related

²³¹ *Id.* (citing FY20 Summary Descriptions, file “PREF-20.docx,” App’x F at F-2). PASS and DSS units allow post offices and other delivery units to capture arrival scans on parcels and identify associated delivery routes. Order No. 6043 at 129 n.204.

²³² Order No. 6043 at 129 (citing FY20 Summary Descriptions, file “CS20-20.docx,” at 20-4). POS ONE units are workstation units used in retail locations. Order No. 6043 at 129 n.205. IMD and MDD scanners are, *inter alia*, used by mail carriers to scan parcels when they are delivered. *Id.*

to PASS, DSS, and POS ONE units and IMD and MDD scanners] are associated with packages.” *Id.*

c. Commission Analysis

UPS does not seriously engage with the Commission’s detailed findings from Order No. 6043 and instead repeats its dissatisfaction with the results of the economically sound methodologies applied by the Commission. UPS continues to assert that costs “associated” with PASS, DSS, and POS ONE units and IMD and MDD scanners are being classified as institutional, but UPS does not allege that any such costs are uniquely or disproportionately associated with Competitive products in an economically sound manner, nor does UPS make any showing that would be sufficient to support such a claim. The Commission has considered the costs associated with package processing and delivery technology and finds that, except for those that are attributed to Competitive products, they are not uniquely or disproportionately associated with Competitive products. Furthermore, even if they were (which they are not), UPS has failed to offer a reasoned basis to alter the formula-based approach to account for these costs, which are significantly less than the formula-based appropriate share (and are significantly less than actual Competitive product contribution to institutional costs).²³³

C. Additional Costs Raised by Commenters

In addition to the costs discussed above, UPS, LI, and ACI raise other types of costs alleged to be “uniquely or disproportionately associated” with Competitive

²³³ The institutional costs associated with equipment depreciation totaled \$276 million in FY 2021. See FY21 Summary Descriptions, file “CS20-21.docx,” at 20-1. This is well below either the formula-based appropriate share for FY 2021 (9.1 percent of institutional costs, or \$3.061 billion) or actual Competitive product contribution to institutional costs in FY 2021 (39.2 percent of institutional costs, or \$13.193 billion). See FY 2021 ACD at 96; FY 2021 ACR at 88-89.

products that were not previously discussed in Order No. 6043. These include costs associated with peak season, rural carriers, vehicle service drivers, and other miscellaneous costs.²³⁴ The Commission considers each of these costs, and, as discussed in greater detail below, concludes that except for those that are attributed to Competitive products, they are not uniquely or disproportionately associated with Competitive products. No commenter offers a reasonable basis to alter the formula-based approach. The Commission's expert judgments on these matters warrant judicial deference because they constitute the "agency's reasoned judgments about technical questions within its area of expertise" that are "reasonable" and "reasonably explained." *UPS I*, 890 F.3d at 1066 (internal mark and citations omitted).

Moreover, even if these cost categories were deemed "uniquely" or "disproportionately" associated by a Federal court reviewing this matter, it would be inappropriate to alter the formula to take these cost categories into account because the Commission's formula-based appropriate share is more than sufficient to ensure coverage. Many of these cost categories are significantly less than the formula-based appropriate share (and are significantly less than Competitive products' actual contribution to institutional costs). Furthermore, the Commission continuously strives to improve cost attribution where it is feasible to do so.²³⁵

²³⁴ UPS Comments at 17-20, 28-29; LI Comments at 1, 3-4; ACI Reply Comments at 2.

²³⁵ See Section VII.B., *supra* (describing recent methodological improvements to cost attribution related to transportation and peak season costs). See also Docket No. RM2022-8, Order on Analytical Principles Used in Periodic Reporting (Proposal Two), September 23, 2022 (Order No. 6280) (approving updates to the attribution of postmaster costs which reduced the amount of institutional costs associated with postmasters by \$41 million). Any interested person may file a petition for the Commission to consider a proposal to change an accepted analytical principle regarding any type of cost. 39 U.S.C. § 3652(e)(2)(A), (C). Additional grounds for data improvement occur when "the quality of service data has become significantly inaccurate or can be significantly improved[.]" which does not apply here. 39 U.S.C. § 3652(e)(2)(B).

1. Peak Season Costs

a. Comments

UPS states that “[t]he costs the Postal Service incurs to ramp up its operations during package peak season are a clear example of costs that are meaningfully associated with package deliveries . . . [,] [y]et the Commission allows the Postal Service to classify many peak season costs as institutional and then claims that, once so classified, their relationship to packages becomes obscure.” UPS Comments at 17. UPS previously raised this issue in a different docket in which it sought changes to the Commission’s costing methodology to account for what UPS termed “unexplained peak-season costs” that UPS alleged were being caused by Competitive products.²³⁶ The Commission rejected UPS’s proposal in that docket after identifying numerous flaws in UPS’s proposed methodology (see *generally* Order No. 6048), and UPS now raises the same concerns in the instant docket. UPS Comments at 18.

UPS states that “[e]very year, the Postal Service . . . must incur significant costs to scale up for package peak season.” UPS Comments at 18. UPS notes that while “[m]any of these peak season costs are attributed to competitive products, . . . [s]ome are classified instead as ‘institutional.’” *Id.* at 19. UPS insists that “these *additional institutional costs* arising from *package peak season* are meaningfully associated with competitive products.”²³⁷ UPS asserts that “[i]f the Postal Service were delivering only the letter mail (which is on a long-term secular decline), it would not incur these significant additional costs to ramp up for package peak season[.]” and “[i]nstitutional

²³⁶ See *generally* Docket No. RM2020-9, Order Rejecting United Parcel Service, Inc.’s Proposed Changes to Postal Service Costing Methodologies (UPS Proposal One), November 29, 2021 (Order No. 6048).

²³⁷ UPS Comments at 20 (emphasis in original). The Commission notes that the correct term for what UPS refers to in its comments as “package peak season” is simply “peak season.” It is not correct that only Competitive product volumes increase during December holiday season. Order No. 6048 at 17-18.

costs would substantially *decline* as a result.” UPS Comments at 20 (emphasis in original). Therefore, according to UPS, “[t]o comply with the [PAEA], the Commission must consider all such costs in setting the appropriate share” *Id.*

ASL asserts that accounting for peak season costs is an issue of cost attribution that is not relevant to the Commission’s appropriate share determination. ASL Reply Comments at 19. ASL argues that peak season costs are properly accounted for by the existing cost attribution methodology and that the peak season costs currently classified as institutional are not uniquely or disproportionately associated with Competitive products. *Id.* at 19-20. ASL states that “consistent with the nature of . . . a multi-product network firm, peak costs include activities associated with the provision of all, or broad groupings of, products that are not caused by individual products.” *Id.* at 20. ASL argues that “UPS does not make any showing that peak costs are ‘uniquely or disproportionately associated’ with Competitive products[] . . . ,” and “in fact[] . . . does not even try to make such a showing, arguing only that the costs are somehow ‘associated’ with Competitive products[,] . . . [which] alone is not enough.” *Id.*

b. Commission Analysis

UPS does not make any showing sufficient to support a claim that the institutional costs incurred during the annual December peak season are uniquely or disproportionately associated with Competitive products in an economically sound manner. The Commission has previously explained why it is incorrect to claim that but for Competitive products the Postal Service would not incur peak season costs. Order No. 6048 at 17-18. Peak season costs are associated not only with Competitive products but also with Market Dominant products that have substantially higher absolute volumes than Competitive products, so that the increases in the volumes of those products produce much higher increases in costs. *Id.* First-Class Mail, for example, also has a December volume peak, and its share of the Postal Service’s overall volume is much larger than Competitive products’ share. *Id.* at 18. The existing costing models

are designed to account for seasonal variation in product volumes. *Id.* at 16-17, 18. The peak season costs that are being classified as institutional under the existing costing methodology consist of network costs (those required to construct and maintain the Postal Service's processing and delivery networks) and costs for activities that are associated with broad groupings of products, not just Competitive products. *Id.* at 20. UPS has not presented anything new or different to demonstrate in an economically sound way why these costs, which the Commission determined in Docket No. RM2020-9 were not incremental to Competitive products, should nevertheless be considered uniquely or disproportionately associated with Competitive products.²³⁸ Upon consideration of the costs associated with peak season, the Commission concludes that, except for those that are attributed to Competitive products, they are not uniquely or disproportionately associated with Competitive products. Furthermore, even if they were (which they are not), UPS has failed to offer a reasoned basis to alter the Commission's formula-based approach to account for these costs, which are significantly less than the formula-based appropriate share (and are significantly less than actual Competitive product contribution to institutional costs).²³⁹

²³⁸ Based on a finding that the Postal Service should accelerate studies on peak season costs, the Commission has initiated a strategic rulemaking to identify priorities for future data collection and analytical work relating to the Postal Service's periodic reports to develop an inventory of data collection and analysis needs, comprehensively evaluate those needs, and devise a plan for meeting those needs with input from any interested persons. See *generally* Docket No. RM2022-1, Notice and Order of Proposed Rulemaking on Periodic Reporting, October 8, 2021 (Order No. 6004). UPS is participating in that proceeding, which remains pending before the Commission. Docket No. RM2022-1, UPS Comments; Docket No. RM2022-1, UPS Reply Comments.

²³⁹ In Docket No. RM2020-9, UPS alleged that the existing costing models fail to explain and attribute on average approximately \$500 million in "additional peak-season costs" annually. Docket No. RM2020-9, Petition of United Parcel Service, Inc. for the Initiation of Proceedings to Make Changes to Postal Service Costing Methodologies, May 29, 2020, at 3. The Commission ultimately rejected UPS's proposal in that docket after concluding that it did not provide any improvement to the current methodology. Order No. 6048 at 2, 32. Nevertheless, the Commission notes that UPS's estimate of \$500 million is well below either the formula-based appropriate share for FY 2021 (9.1 percent of institutional costs, or \$3.061 billion) or actual Competitive product contribution to institutional costs in FY 2021 (39.2 percent of institutional costs, or \$13.193 billion). See FY 2021 ACD at 96; FY 2021 ACR at 88-89.

2. Rural Carrier Costs and Vehicle Service Driver Costs

a. Comments

UPS asserts that between FY 2018 and FY 2021, rural carrier costs increased \$1.2 billion (15 percent), while the institutional portion of rural carrier costs increased \$680 million (13 percent), “an increase that cannot be explained by falling mail volumes, modest increases in delivery points, or inflation.” UPS Comments 28. UPS states that “[t]he obvious implication is that it is associated with the growth of competitive products.” *Id.* Likewise, UPS asserts that between FY 2018 and FY 2021 vehicle service driver costs increased \$154 million (20 percent), while the institutional portion of vehicle service driver costs increased 9 percent. *Id.* at 29.

b. Commission Analysis

UPS does not make any showing sufficient to support a claim that recent increases in the institutional portion of rural carrier costs or vehicle service driver costs are uniquely or disproportionately associated with Competitive products in an economically sound manner. The mere fact that total rural carrier costs and the institutional portion of rural carrier costs both increased, or that total vehicle service driver costs and the institutional portion of vehicle service driver costs both increased, is not, on its own, sufficient to establish any relationship or association between these costs and Competitive products. And even if some link between the increase in the institutional portion of rural carrier costs or vehicle service driver costs and Competitive products were established, that would still fall well short of showing that the institutional portion of rural carrier costs or vehicle service driver costs was uniquely or disproportionately associated with Competitive products. The Commission has considered the costs associated with rural carriers and vehicle service drivers and finds that, except for those that are attributed to Competitive products, they are not uniquely or disproportionately associated with Competitive products.

3. Other Types of Costs

a. Comments

LI asserts that “it is essential that the [Commission] fundamentally change its approach to, and methodology for determining, institutional cost contributions/attributions and the calculation of appropriate share pertaining to competitive products.” LI Comments at 1. According to LI’s calculations, “approximately 87 percent of [delivery] vehicle space is used for competitive products[,]” and “[g]iven this disproportionate use of vehicle space by competitive products/packages, the overwhelming majority of vehicle costs should be applied to competitive products as well as other costs involved in processing and delivering competitive products.” *Id.* at 3-4. LI also cites “[a]dditional factors supporting this change[,]” including “the labor-intense nature of package delivery; packages’] intermittent delivery schedule (i.e., not to every address on every day); [packages’] higher injury rates and disability claims than mail; and their seven-day-a-week delivery window compared to mail’s six-day window.” *Id.* at 4.

ACI accuses the Postal Service of “an apparent pervasive regime of shifting costs and risk from competitive services to market dominant services” ACI Reply Comments at 2 (internal marks omitted). ACI states that “[i]ncreases in postal costs, including institutional costs, are driven by the competitive shipping and package segment, as evidenced by the fact that packages now occupy the majority of the space on delivery vehicles.” *Id.* According to ACI, “[t]his shift has led to increases in fixed overheads . . . [y]et, only 8.8% of institutional costs are allocated to these competitive services.” *Id.* Furthermore, “because post offices are generally closed on Sundays while delivery of packages carries on, the allocation of institutional costs to competitive packages should include another 14.3% of costs – reflecting one of seven days of operations that exclusively use these overheads.” *Id.* ACI states that “the Commission should validate this with an intelligible formula . . . [and] must adopt rules that ensure

that competitive products absorb a commensurate degree of institutional costs, relative to the stresses that the product segments convey.” *Id.*

b. Commission Analysis

With respect to LI’s call for the Commission to “fundamentally change” its approach to determining the appropriate share, the Commission notes that the bases referenced by LI to support taking such action (*i.e.*, “dramatic changes in recent years with the U.S. Postal Service’s revenue composition, product, and service mix”²⁴⁰), are not nearly as “dramatic” as LI asserts, and have been fully accounted for by the Commission in developing the formula-based approach to setting the appropriate share. While Competitive product revenue for the Postal Service has increased significantly in recent years, this must be viewed within the context of the overall market for Competitive postal products having expanded significantly, which has benefitted all market participants.²⁴¹ From FY 2017 to FY 2021, the Postal Service’s Competitive product revenue increased approximately 65.5 percent, but the Postal Service’s share of the market for competitive postal services only increased by approximately 1 percentage point, and Competitive products went from constituting only about 3.4 percent of total mail volume to approximately 5.6 percent by the end of FY 2021.²⁴² The Postal Service’s competitors still control approximately 79.6 percent of the market for competitive postal services. See Section V.B.2.b., *supra*, Table V-4. The revenue growth that has occurred has been substantially driven by heightened demand in the

²⁴⁰ LI Comments at 1.

²⁴¹ See Section V.B.2.b., *supra*. As explained at Section IV.B.2., *supra*, the Commission interprets the appropriate share requirement to function not primarily as a costing requirement, but to prevent any potential market imbalance arising from the Postal Service’s pricing decisions with respect to its Competitive products. Therefore, the growth in Competitive product revenue is relevant to the Commission’s consideration not just of the Postal Service, but of the market for competitive postal services more broadly.

²⁴² Compare FY 2017 Financial Report, App’x A, with FY 2021 Financial Report, App’x A. See also Section V.B.2.b., *supra*, Table V-4.

market for competitive postal services, which has enabled all competitors to increase their prices. See Section V.B.2.b., *supra*.

The Commission has thoroughly explained how the existing costing methodology, which has evolved incrementally over more than 50 years and continues to be refined and improved consistent with the relevant statutory criteria and sound economic and cost accounting principles, is designed to facilitate the attribution of costs to products or groups of products to the greatest extent feasible. Order No. 6043 at 11-34. The Commission has also thoroughly explained how the formula-based approach to determining the appropriate share fully accounts for the relevant statutory criteria, given the appropriate share's purpose as a minimum contribution level intended to prevent or correct any competitive imbalance in the market due to the Postal Service's pricing decisions. *Id.* at 46-47, 59-62, 103-05. This includes both the prevailing competitive conditions in the market and the degree to which any costs are uniquely or disproportionately associated with any Competitive products. *Id.* at 72-97, 105-09; see 39 U.S.C. § 3633(b). Rather than meaningfully engage with the Commission's detailed findings in Order No. 6043 or with the Commission's cost attribution dockets, LI suggests that the Commission completely replace the formula-based approach to determining the appropriate share without any evidence that doing so is necessary or would be appropriate or consistent with the relevant statutory provisions at issue, and without suggesting any specific alternative.

LI's assertion that "approximately 87 percent of [delivery] vehicle space is used for competitive products" is based on a highly misleading calculation. Using a ratio extrapolated from public testimony by the Postmaster General before a congressional subcommittee to the effect that "from a cubic movement standpoint . . . a tractor trailer of mail would hold 500,000 pieces; a tractor trailer of packages would hold 5,000

pieces[.]”²⁴³ LI concludes that “the average package is 100 times the size of the average letter[.]” a ratio of 100:1. LI Comments at 3. Then, using a ratio obtained from regulatory filings by the Postal Service, LI estimates that in FY 2021 the Postal Service delivered 15 times more mail (at 120.6 billion pieces) than packages (at 8.0 billion pieces), a ratio of 15:1. *Id.* LI divides the 100:1 ratio by the 15:1 ratio to conclude that packages take up 6.6 times more space than letters. *Id.* Using this figure, LI then arrives at its conclusion that “approximately 87 percent of vehicle space is used for competitive products.” *Id.*

The Postmaster General was testifying about *tractor trailers* used to transport mail between postal processing facilities, not the delivery vehicles which the Postal Service is currently in the process of replacing, and was speaking with respect to *maximum capacities*, not the amount of mail actually being carried on mail delivery vehicles. As a result, even if LI’s figures were correct, this information would have no bearing on the question of what amount of delivery vehicle costs should be attributed to, or are uniquely or disproportionately associated with, Competitive products.²⁴⁴

Other grounds cited by LI for its argument that “the overwhelming majority of vehicle costs should be applied to competitive products as well as other costs involved in processing and delivering competitive products” are: “the labor-intense nature of package delivery; packages['] intermittent delivery schedule (i.e., not to every address on every day); their higher injury rates and disability claims than mail; and their seven-day-a-week delivery window compared to mail’s six-day window.” LI Comments at 4. However, as the Commission has explained, the existing costing methodology accounts

²⁴³ *Hearing on Oversight of the U.S. Postal Service Before the Subcomm. on Fin. Servs. and Gen. Gov’t of the H. Comm. on Appropriations*, 117th Cong. 22:07 (Mar. 11, 2021) (testimony of Louis DeJoy, Postmaster General, United States Postal Service), available at <https://appropriations.house.gov/events/hearings/oversight-of-the-us-postal-service>.

²⁴⁴ The Commission also notes that there is no way to verify what data the Postmaster General was relying on in giving this testimony.

for the fact that Competitive products are often larger and heavier, and hence more labor-intensive to process and deliver, than Market Dominant products. Order No. 4963 at 139. Cost drivers include mail characteristics such as weight and shape (e.g., letters or parcels), and costs are distributed to products in proportion to the prevalence of the cost driver within each product. *Id.* Thus, heavier Competitive products have more weight-driven costs attributed to them than lighter products. *Id.* In FY 2021, the more labor-intensive nature and higher weight-related costs of parcels was reflected in the cost attribution, with the average cost-per-piece attributed to Competitive products being approximately \$2.90. FY 2021 Financial Report, App'x A. In contrast, the average cost-per-piece attributed to Market Dominant products was only 21.3 cents. *Id.*

The fact that packages are not delivered to every address on every day has no effect on the Postal Service's institutional costs, as the Postal Service's network is designed to service every address 6 days a week regardless of mail volume or mail mix. Workers' compensation costs resulting from current-year workplace injuries are volume-variable in the same proportions as composite labor costs and distributed to products in the same proportions as composite labor costs. FY21 Summary Descriptions, file "CS18-21.docx," at 18-16. As a result, any added workers' compensation cost due to higher injury rates associated with Competitive products would be disproportionately attributed to Competitive products. The fact that Competitive products, unlike Market Dominant products, are delivered on Sunday is accounted for by the existing costing methodology, which attributes the vast majority of the costs of Sunday delivery to Competitive products.²⁴⁵

²⁴⁵ See FY 2021 Summary Descriptions file "CS07-21.docx" at 7-6. In FY 2021, 98.5 percent of costs associated with Cost Segment 7.2.3 ("Sunday/Holiday Delivery") were attributed to Competitive products. See Docket No. ACR2021, Library Reference USPS-FY21-NP10, December 29, 2021, folder "Model," Excel file "IC2021NP.IC.xlsx," tab "CS07;" Library Reference PRC-LR-ACR2021-1, Excel file "FY21Public.B.xlsx," tab "CS07." The specific percentages were calculated by Commission staff using the data from these worksheets.

ACI similarly asserts that “packages now occupy the majority of the space on delivery vehicles[.]” but without citing any evidence for this claim. ACI Reply Comments at 2. To the extent that ACI is arguing that the appropriate share should be increased in response to increases in Competitive product volumes and/or disproportionate use of delivery vehicles by Competitive products, as the Commission has explained, the institutional portion of vehicle depreciation costs is made up of depreciation costs associated with non-delivery-related administrative vehicles, as well as the depreciation costs associated with delivery-related vehicles with respect to activities that do not vary with volume (such as driving from mailbox to mailbox), or simply due to all forms of normal depreciation. Order No. 6043 at 116-17. ACI does not present any evidence (other than this single unverifiable statement) to show that any of these institutional costs are uniquely or disproportionately associated with Competitive products, and hence that the appropriate share should be increased to reflect them.

ACI claims that increased Competitive product volumes have “led to increases in fixed overheads[.]” by which ACI presumably means institutional costs, but, again, ACI does not cite any evidence for this, and as explained *infra* at Sections VIII.B.3. and VIII.D.3., no correlation exists between increases in Competitive product volumes and changes in institutional costs. ACI Reply Comments at 2. ACI asserts that one-seventh of institutional costs (14.3 percent) should be allocated to Competitive products because unlike Market Dominant products, Competitive products are delivered on Sundays; hence ACI appears to presume that one-seventh of all institutional costs accrue on Sundays, and that all such costs are associated with Competitive products. *Id.* The problem with this argument, however, is that very few delivery-related institutional costs

accrue on Sundays, since the vast majority of the total costs of Sunday delivery are attributed to Competitive products.²⁴⁶

ACI argues that “the Commission must . . . ensure that Competitive products absorb a commensurate degree of institutional costs, relative to the stresses that the product segments convey.” ACI Reply Comments at 2. However, as the Commission details in addressing UPS’s proposed alternatives to setting the appropriate share, no meaningful relationship exists between increases in Competitive product volumes and changes in institutional costs, and any attempt to force the allocation of institutional costs to Competitive products would be arbitrary and have harmful effects similar to fully distributed costing, in contravention of the PAEA. See Sections VIII.A.3., VIII.B.3., VIII.C.3., VIII.D.3., *supra*.

Finally, the Commission rejects ACI’s general contentions that the Postal Service is improperly “shifting costs . . . from competitive services to market dominant services” ACI Reply Comments at 2. The Commission has already discussed the statutory interpretation and technical flaws on which this mistaken assumption is based. See Sections IV.B.2., V.A.3.b., *supra*.

The Commission has considered the costs raised by these commenters and finds that, except for those that are attributed to Competitive products, they are not uniquely or disproportionately associated with Competitive products. Furthermore, even if they were (which they are not), these commenters have failed to offer a reasoned basis to alter the Commission’s formula-based approach. The costs of Sunday delivery are virtually all already attributed to Competitive products, and the other costs raised by

²⁴⁶ See FY 2021 Summary Descriptions file “CS07-21.docx” at 7-6. In FY 2021, 98.5 percent of costs associated with Cost Segment 7.2.3 (“Sunday/Holiday Delivery”) were attributed to Competitive products. See Docket No. ACR2021, Library Reference USPS-FY21-NP10, folder “Model,” Excel file “IC2021NP.IC.xlsx,” tab “CS07;” Library Reference PRC-LR-ACR2021-1, Excel file “FY21Public.B.xlsx,” tab “CS07.” The specific percentages were calculated by Commission staff using the data from these worksheets.

these commenters are significantly less than both the formula-based appropriate share (as well as actual Competitive product contribution to institutional costs).²⁴⁷

VIII. ALTERNATIVES RAISED BY COMMENTERS

A. Attributable Cost Shares

1. Introduction

Throughout this proceeding, UPS has suggested that the best proxy for the appropriate share level would be for Competitive products to contribute to institutional costs in the same proportion at which they contribute to total attributable costs.²⁴⁸ In prior orders, the Commission considered and rejected UPS's proposal that the appropriate share be based on Competitive products' attributable cost shares. Order No. 4402 at 80-82; Order No. 4963 at 36. The Commission explained that the use of attributable cost shares in determining the appropriate share would produce an outcome "tantamount to fully-allocated costing." Order No. 4402 at 81-82; Order No. 4963 at 36.

²⁴⁷ It is not necessarily clear precisely which costs these commenters are referring to. LI alleges generally that "the overwhelming majority of *vehicle costs* should be applied to competitive products as well as other costs involved in processing and delivering competitive products." LI Comments at 3-4 (emphasis added). ACI alleges even more generally that increases in institutional costs are being driven by Competitive products. ACI Reply Comments at 2. Even if "vehicle costs" are deemed to extend beyond vehicle depreciation to also include fuel and maintenance, the aggregate institutional costs associated with those activities in FY 2021 were \$836.2 million. See FY21 Summary Descriptions, file "CS12-21.docx," at 12-1, Cost Components 12.2 and 12.3; FY21 Summary Descriptions, file "CS20-21.docx," at 20-1, Cost Component 20.2. The total institutional cost associated with mail processing in FY 2021 was \$705 million. See FY21 Summary Descriptions, file "CS03-21.docx," at 3-1. These are both well below either the formula-based appropriate share for FY 2021 (9.1 percent of institutional costs, or \$3.061 billion) or actual Competitive product contribution to institutional costs in FY 2021 (39.2 percent of institutional costs, or \$13.193 billion). See FY 2021 ACD at 96; FY 2021 ACR at 88-89.

²⁴⁸ See, e.g., UPS Order No. 3624 Comments at 34-35; Initial Comments of United Parcel Service, Inc. on Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products, April 16, 2018, at 36, 40; Comments of United Parcel Service, Inc. on Revised Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products, September 12, 2018, at 50-53, 56; Declaration of J. Gregory Sidak on Behalf of United Parcel Service, September 12, 2018, at 37-39.

The Commission elaborated that the use of attributable cost shares would base the appropriate share on considerations different from those set forth in 39 U.S.C. § 3633(b) as relevant circumstances because adopting such a proposal would not provide any insight into market power, the size of the parcel delivery market, or any other prevailing competitive conditions or relevant circumstances. Order No. 4402 at 81; Order No. 4963 at 36.

In response to Order No. 6043, UPS restates its proposal to set Competitive products' appropriate share by reference to their share of the Postal Service's total attributable costs. UPS Comments at 41-48. ASL, Pitney Bowes, the Postal Service, and the Public Representative oppose UPS's proposed use of attributable cost shares as the basis for the appropriate share requirement.²⁴⁹ ASL's opposition relies (in part) on analysis performed by Dr. Panzar, Louis W. Menk Professor of Economics, Emeritus at Northwestern University. See ASL Reply Comments at 1; Panzar Reply Decl. at 2, 3-6, 17.

2. Comments

UPS repeats that "[t]he most straightforward way to set the appropriate share in compliance with the [PAEA] is to set the share at or around the same level as the share of overall attributable costs." UPS Comments at 41; see UPS Reply Comments at 31. UPS contends that the use of attributable cost shares "best fulfills the statutory mandates of recovering costs, avoiding subsidization, and protecting fair competition." UPS Comments at 42; see UPS Reply Comments at 31. UPS asserts that if attributable cost shares were used it would "result in the math adding up to 100%" for institutional costs and allow for the allocation of total institutional costs between Market Dominant and Competitive products, which it further asserts is a requirement of 39 U.S.C.

²⁴⁹ See ASL Reply Comments at 21-22; Pitney Bowes Reply Comments at 11-13; Postal Service Reply Comments at 52-60; PR Reply Comments at 9-13.

§ 3622(b)(9). UPS Comments at 42. UPS argues its approach is “more rigorous and economically sound than the formula the Commission proposes.” *Id.* at 42-43. UPS asserts that, if the Commission’s conclusion that there is no meaningful way to separate institutional costs and assign them to Competitive products is true, “then the proper approach is simply to extend the Commission’s rigorous analysis of attributable costs to institutional costs” *Id.* at 43. UPS argues that using attributable cost shares “would ensure that competitive products recover their fair share” of institutional costs. *Id.* UPS claims that using attributable cost shares does not constitute fully distributed costing because it does not assign costs to individual products. *Id.* at 43-44.

As a threshold matter, the Public Representative rejects UPS’s claim that 39 U.S.C. § 3622(b)(9) requires the Commission to distribute the Postal Service’s total institutional costs between Market Dominant and Competitive products. PR Reply Comments at 9. He observes that 39 U.S.C. § 3622(b)(9) does not contain such a requirement and is only one of nine objectives used to govern Market Dominant rate regulation. *Id.* He further notes that “[n]one of the nine objectives impose ‘requirements’ as alleged by UPS.” *Id.* (citing 39 U.S.C. § 3622(b)).

The Postal Service asserts that UPS’s attributable cost shares approach fails to consider the relevant statutory factors. Postal Service Reply Comments at 60. The Postal Service contends that UPS’s proposal “would totally eliminate the Commission’s ability to comply with its obligation to consider . . . ‘prevailing competitive conditions in the market’ . . . (or any other ‘relevant circumstances’).” *Id.* at 56. Furthermore, it contends that UPS seeks to “blur costing and pricing,” in direct conflict with the Supreme Court’s decision in *National Association of Greeting Card Publishers v. United States Postal Service*, 462 U.S. 810 (1983), which the Postal Service maintains held a critical distinction between prohibited efforts to allocate unattributed costs based on cost-of-service principles and that these costs should be recovered based on discretionary pricing factors. *Id.* at 56-58. The Postal Service also disagrees with

UPS's argument that using attributable cost shares "'adheres more faithfully' to the PAEA," observing that 39 U.S.C. § 3633(b) specifies a unique or disproportionate association rather than merely an association. *Id.* at 58-59 (quoting UPS Comments at 45).

Similarly, noting that "UPS attempts to wave away" the PAEA's requirement to consider costs that are "uniquely or disproportionately associated" rather than merely associated, Pitney Bowes asserts that the underlying basis for any such association is arbitrary. Pitney Bowes Reply Comments at 13. Dr. Panzar states that, "[i]n addition to attributable costs, many other economically relevant product-level quantities come to mind: e.g., volumes, revenues, cubic inches, weight, etc." Panzar Reply Decl. at 6. Dr. Panzar explains that the appropriate share could easily be set based on the relative share of any of those quantities, all ending in different appropriate share levels. *Id.* As a result, Dr. Panzar maintains, "choosing any particular allocation rule would be inherently arbitrary" *Id.*

Overall, the Postal Service, ASL, Dr. Panzar, and Pitney Bowes reject UPS's proposed use of attributable cost shares because it is tantamount to fully distributed costing, and thereby would result in the arbitrary allocation of costs.²⁵⁰ The Postal Service rebuts UPS's claim that using attributable cost shares is not fully distributed costing because the specific distribution of institutional costs to individual Competitive products would be left to the Postal Service. Postal Service Reply Comments at 55. The Postal Service observes that using attributable cost shares would result in the distribution of all the Postal Service's costs and that "one obvious hallmark of fully distributed costing is the absence of any residual institutional costs left to be recovered on the basis of discretionary pricing factors." *Id.* The Postal Service adds that, if all costs originally classified as institutional were "mechanistically" distributed to Market

²⁵⁰ See Postal Service Reply Comments at 54; ASL Reply Comments at 21; Panzar Reply Decl. at 6; Pitney Bowes Reply Comments at 11.

Dominant and Competitive products, “then nothing is left to be evaluated in the manner in which institutional costs were intended to be evaluated in the pricing process -- particularly, in this context, in the setting of the appropriate share under subsection 3633(a)(3).” *Id.*

Finally, Pitney Bowes adds that using attributable cost shares as proposed by UPS is economically unsound. Pitney Bowes Reply Comments at 11-12. The Public Representative observes that using attributable cost shares of Competitive and Market Dominant products, whereby 100 percent of institutional costs would be recovered, involves only a “simple arithmetic pro-rationing of institutional costs” based on attributable cost shares. PR Reply Comments at 10. The Public Representative contends “[t]his would by no means be ‘more rigorous’ or ‘economically sound’” when compared to the Commission’s formula. *Id.*

3. Commission Analysis

The Commission previously considered and rejected a proposal by UPS to set the appropriate share based on Competitive products’ attributable cost shares. Order No. 4402 at 80-82; Order No. 4963 at 36. In response to Order No. 6043, UPS restates its proposal to set Competitive products’ appropriate share by reference to their share of the Postal Service’s total attributable costs. UPS Comments at 41-48; UPS Reply Comments at 31. The Commission again rejects UPS’s proposed use of attributable cost shares because this proposal is inconsistent with the applicable statutory criteria, is arbitrary, and is economically unsound as discussed in detail below.

First, UPS claims that its attributable cost share approach is consistent with the statutory criteria and adheres to the PAEA more faithfully than the status quo. See UPS Comments at 45. This claim is incorrect. UPS interprets 39 U.S.C. § 3622(b)(9) as a requirement that the Postal Service allocate *all* its institutional costs between Market Dominant and Competitive products. See *id.* at 42; 39 U.S.C. § 3622(b)(9). As

explained in Section IV.D.2., *supra*, 39 U.S.C. § 3622(b)(9) constitutes one of nine objectives that the Commission must consider in conjunction with each other whenever it establishes, revises, modifies, or adopts an alternative ratemaking system for Market Dominant products; 39 U.S.C. § 3622(b)(9) does not apply to (or require any regulatory action with respect to) the Competitive product ratemaking system. *See generally* 39 U.S.C. § 3622; *see also* PR Reply Comments at 9. By contrast, 39 U.S.C. § 3633(a)(3) and (b) govern Competitive products' contribution to institutional costs, and neither provision requires the total allocation of the Postal Service's institutional costs. *See* 39 U.S.C. § 3633(a)(3), (b). UPS's interpretation of 39 U.S.C. § 3622(b)(9) is fundamentally flawed because if allocating all the Postal Service's institutional costs was indeed a requirement, then it would produce a statutory conflict with 39 U.S.C. § 3633(b), which unambiguously authorizes the Commission to eliminate the appropriate share.²⁵¹

Moreover, the use of UPS's attributable cost share approach would fail to "consider all relevant circumstances, including the prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products," as required by 39 U.S.C. § 3633(b). *See* 39 U.S.C. § 3633(b). This is because the Postal Service's attributable cost shares do not allow for consideration of the Postal Service's market power, the size of the overall parcel delivery market, or any other "prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products." *See id.* Under UPS's proposal, all institutional costs are allocated in a mechanical manner, without any consideration of the relevant circumstances as required by 39 U.S.C. § 3633(b). *See* UPS Comments at 41-48; *see*

²⁵¹ Compare 39 U.S.C. § 3622(b)(9), with 39 U.S.C. § 3633(b). *See* Pitney Bowes Reply Comments at 6.

a/so 39 U.S.C. § 3633(b). Thus, UPS's attributable cost share approach is inconsistent with the applicable statutory criteria.

Second, although UPS's proposed use of attributable cost shares may appear straightforward, allocating institutional cost based on attributable cost is arbitrary. The Commission could just as easily allocate institutional costs based on revenue shares²⁵² or volume shares,²⁵³ or, as Dr. Panzar notes, based on some other "economically relevant product-level quantities[.]" such as cubic inches or weight. Panzar Reply Decl. at 6. All these alternative approaches are equally straightforward, but all produce substantially different results, which is why the application of any of them would be unreasonable. With no rational basis for preferring one approach over another, an arbitrary selection can create vastly differing impressions of the financial viability of the products. See Order No. 6043 at 90. Such distortions of accurate costing would be inconsistent with the PAEA (see Section IV.B.2., *supra*) and form the basis of a real risk that adopting such an approach to regulation may distort fair competition and harm consumers. See Order No. 6043 at 87-92.

UPS provides no justification for choosing attributable cost shares as the basis for determining the appropriate share of institutional costs for Competitive products. Instead, UPS implies that because the Commission's attributable cost analysis is the best means of determining the percentages of attributable costs to assign to both Market Dominant and Competitive products, it is therefore reasonable to use attributable cost shares for assigning institutional cost to those products. See UPS Comments at 43. Essentially, UPS proposes that the Commission treat institutional costs in the same way that it treats indirect costs, *i.e.*, by piggybacking institutional costs

²⁵² This refers to the proportion of Market Dominant or Competitive products' revenue relative to the Postal Service's total revenue. The Commission considered and rejected UPS's proposal to base the appropriate share on Competitive products' revenue. Order No. 4402 at 80-82.

²⁵³ This refers to the proportion of Market Dominant or Competitive products' volume relative to the Postal Service's total volume. See, *e.g.*, Order No. 6043 at 89-91; Panzar Reply Decl. at 6.

on attributable costs.²⁵⁴ With piggybacking, the Commission can attribute some indirect costs to products by exploiting the relationships between cost components. However, the Commission's attribution of indirect costs and UPS's attributable cost share approach fundamentally differ. There is a discernable relationship between direct and indirect costs which the Commission's methodology relies upon to attribute indirect costs to products. UPS attempts to mimic the same method here to piggyback institutional costs onto attributable costs, even though no relationship between institutional costs and attributable costs exists.

For example, under the Commission's attribution methodology, for mail processing costs, piggyback costs augment labor cost estimates by adding the costs associated with supervisors and administration, service-wide benefits, and facility-related and equipment-related costs. While these costs do not directly vary with volume, changes in volume affect the amount of direct labor needed to process the mail, which in turn affects the number of supervisors that are needed to oversee operations, the cost of service-wide benefits, and the facility-related and equipment-related costs associated with employees working in mail processing operations.

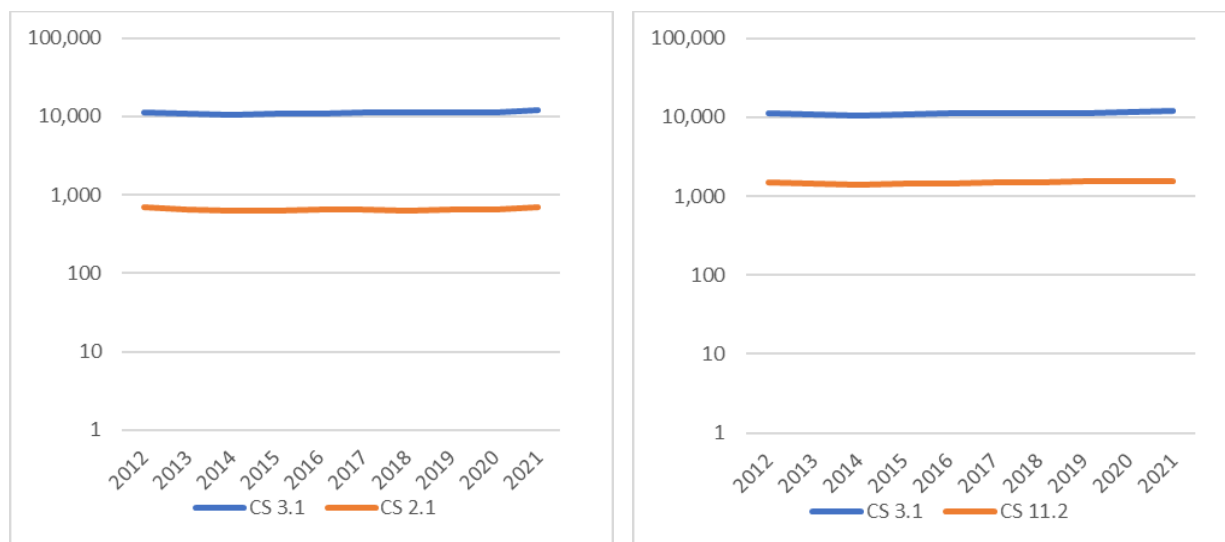
Below, Figure VIII-1 illustrates the relationship between mail processing direct labor costs (Cost Component 3.1)²⁵⁵ and two categories of indirect costs that are piggybacked onto mail processing direct labor costs—cost of supervision of mail

²⁵⁴ Detailed information regarding piggybacking appears in FY21 Summary Descriptions, file "APPH-21.docx," at H-5.

²⁵⁵ "This component encompasses three major categories of activities: 1) automated and manual distribution of mail; 2) "allied labor" operations (including platform operations, collection and cancellation operations, mail preparation, manual bundle/tray/sack sorting, and dispatching); and 3) miscellaneous work including bulk mail acceptance, specialized operations for Priority Mail Express, Registered Mail, and Business Reply Mail, and other mail processing support activities." FY21 Summary Descriptions, file "CS03-21.docx," at 3-3.

processing operations (Cost Component 2.1)²⁵⁶ and operating equipment maintenance costs (Cost Component 11.2).²⁵⁷

**Figure VIII-1
Comparison of Cost Segment Costs,
FY 2012–FY 2021
(Millions of Dollars)**



Source: Postal Service Cost Segments and Components Reports, FY 2012–FY 2021.

²⁵⁶ “This component includes costs associated with the direct supervision of mail processing operations, including central mail mark-up.” FY21 Summary Descriptions, file “CS02-21.docx,” at 2-5.

²⁵⁷ “Operating equipment maintenance costs are for personnel responsible for the maintenance of mail processing equipment, Point of Service (POS ONE), Intelligent Mail Devices (IMDs) and Mobile Delivery Devices (MDDs), and other window service and computer equipment. Costs for equipment maintenance are developed separately for 26 types of equipment from engineering and expense account records.” FY21 Summary Descriptions, file “CS11-21.docx,” at 11-4 (footnote omitted).

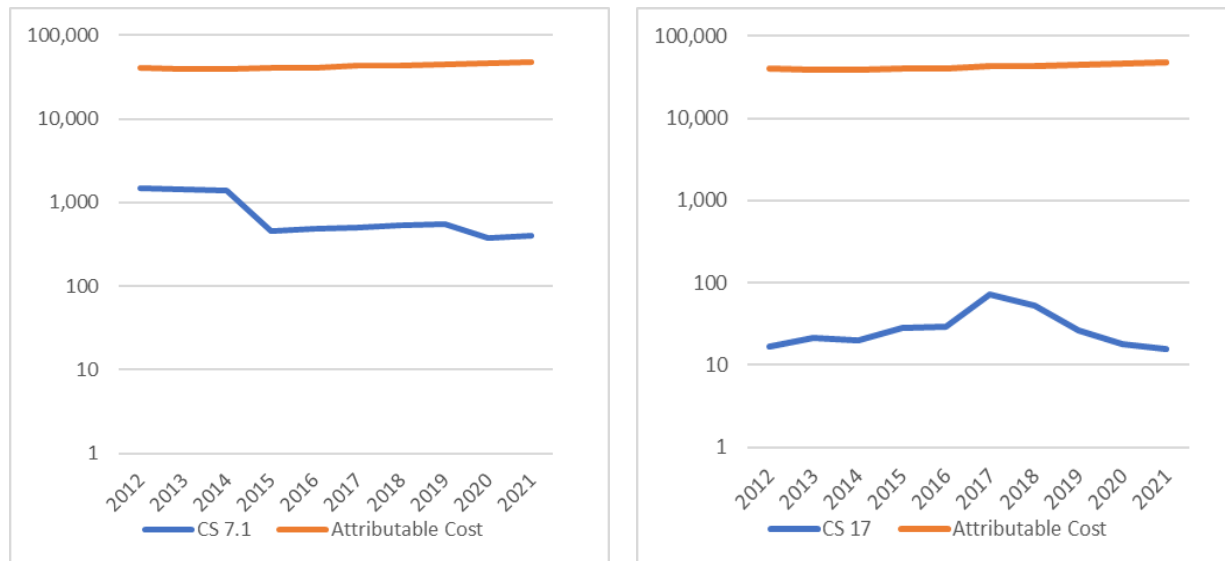
As Figure VIII-1 shows, the costs of both Cost Components 2.1 and 11.2 closely track the primary cost component, Cost Component 3.1. Thus, the Commission's assumption that the indirect costs of Cost Components 2.1 and 11.2 vary with volume to the same extent that direct labor costs of Cost Component 3.1 vary with volume is supported by the fact that these costs have moved in tandem throughout the last decade.

For comparison, the Commission presents two examples to illustrate trends in institutional costs compared with attributable costs. The examples present a cost segment and a cost component that contain only fixed costs that are easily identifiable and discrete. The examples are network travel cost (Cost Component 7.1)²⁵⁸ and research and development cost (Cost Segment 17).²⁵⁹ Below, Figure VIII-2 illustrates the relationship between these two categories of discrete fixed costs and the Postal Service's total attributable costs.

²⁵⁸ "Network travel is time traveling a letter route that is unrelated to volume. . . . [It] is the time spent traveling between delivery sections." FY21 Summary Descriptions, file "CS07-21.docx," at 7-3.

²⁵⁹ "This segment covers the accrued costs for materials, equipment, and contract services relating to research and development (R&D). R&D expenditures are incurred primarily for developmental efforts to improve mail processing technology, construction engineering, and field industrial engineering." FY21 Summary Descriptions, file "CS17-21.docx," at 17-1.

Figure VIII-2
Comparison of Cost Segments and Attributable Costs,
FY 2012–FY 2021
(Millions of Dollars)

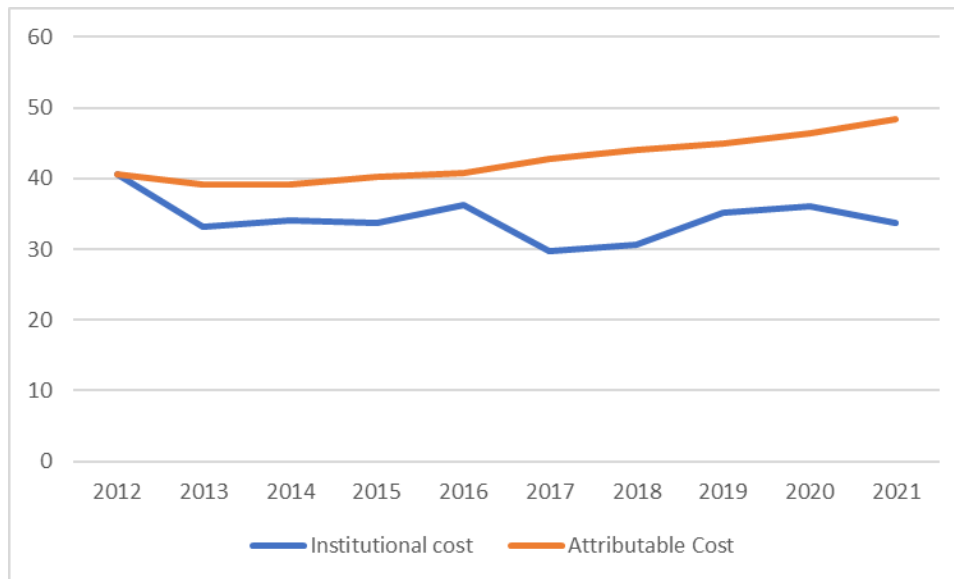


Source: Postal Service Cost Segments and Components Reports, FY 2012–FY 2021.

As Figure VIII-2 shows, unlike the piggybacked costs presented in Figure VIII-1, *supra*, which move in tandem with applicable direct costs, both categories of institutional costs behave differently than attributable costs.

Below, Figure VIII-3 illustrates the relationship between the Postal Service's total institutional costs and total attributable costs.

Figure VIII-3
Comparison of Attributable and Institutional Costs,
FY 2012–FY 2021
(Billions of Dollars)



Source: Docket No. ACR2012, *Annual Compliance Determination* (Revised), May 7, 2013 (FY 2012 ACD); Docket No. ACR2013, *Annual Compliance Determination*, March 27, 2014 (FY 2013 ACD); Docket No. ACR2014, Library Reference PRC-LR-ACR2014/1, March 27, 2015; Docket No. ACR2015, Library Reference PRC-LR-ACR2015/1, March 28, 2016; Docket No. ACR2016, Library Reference PRC-LR-ACR2016/1, March 28, 2017; Docket No. ACR2017, Library Reference PRC-LR-ACR2017-1, March 29, 2018; Docket No. ACR2018, Library Reference PRC-LR-ACR2018-1, April 12, 2019; Docket No. ACR2019, Library Reference USPS-FY19-1, December 27, 2019; Library Reference PRC-LR-ACR2020-1; Library Reference PRC-LR-ACR2021-1.

As Figure VIII-3 shows, the result is the same when comparing institutional costs in the aggregate with total attributable costs. This is because institutional costs are not driven by attributable costs, nor are they driven by a common factor or cause. This result is to be expected, because attributable costs are those that are caused by the provision of products or groups of products, while institutional costs are those that are not. Since the costs are segregated based on what causes them, the resulting two groups of costs change independently of each other. The relationship between

attributable costs and institutional costs that UPS relies upon to allocate institutional costs to Competitive products does not exist.

Third, regardless of how UPS characterizes its approach, use of attributable cost shares as the basis for the appropriate share requirement suffers from the same defects displayed by fully distributed costing. Previously, the Commission explained that use of attributable cost shares was a form of fully distributed costing (see Order No. 4402 at 81), which occurs when the costs of a multi-product firm are assigned or allocated to the individual products or services produced by that firm. See 2020 Panzar Paper at 8; see *also* Order No. 6043 at 85. Under this methodology, attributable costs of products and services are determined and then subtracted from the total costs of the firm, leaving only residual costs, *i.e.*, institutional costs, which are then allocated to products on an arbitrary basis. Order No. 6043 at 85.

UPS objects to this characterization because, unlike most applications of fully distributed costing, it suggests the allocation of costs to Competitive products collectively, instead of at the product level. UPS Comments at 43-44. Other commenters dispute UPS's strict interpretation of fully distributed costing and concur that implementing UPS's attributable cost shares approach would display fundamental flaws like the adoption of fully distributed costing.²⁶⁰ For example, the Postal Service notes that "one obvious hallmark of fully distributed costing is the absence of any residual institutional costs left to be recovered on the basis of discretionary pricing

²⁶⁰ ASL Reply Comments at 22 (explaining that implementing UPS's attributable cost shares approach "would arbitrarily allocate institutional costs like [fully distributed costing]" and that UPS's objection that its approach would not assign all costs to *individual* products is "a distinction without a difference"); Pitney Bowes Reply Comments at 11-13 (explaining that UPS's attributable cost shares approach mirrors and has the same economic drawbacks as fully distributed costing); Panzar Reply Decl. at 6 (explaining that "choosing any particular allocation rule [to implement UPS's attributable cost shares approach] would be inherently arbitrary – exactly as under fully distributed costing, or FDC"); PR Reply Comments at 12 ("Whether or not pro-rationing of institutional costs is fully distributed costing, it is nothing less than a form of extended cost attribution rejected long ago by the Commission and the courts."); Postal Service Reply Comments at 55 ("The routine protestations by UPS on pages 43-45 that this proposal would not constitute fully distributed costing do not withstand scrutiny.").

factors.” Postal Service Reply Comments at 55. It argues that because UPS’s methodology allocates all institutional cost, it is equivalent to fully distributed cost. See *id.* The Commission agrees. As the Commission explained in Order No. 6043, “[t]his purported distinction is irrelevant because the effect on Competitive products of adopting the UPS approach would be functionally identical to adopting fully distributed costing.” Order No. 6043 at 85 n.130. UPS’s approach shares the same defects as fully distributed costing, namely that the choice of allocation method is arbitrary, and when used to develop prices, it can lead to prices that do not reflect the appropriate economic signals. See *id.* at 87-92. Adopting UPS’s approach could force the Postal Service to set prices well above competitive levels. See *id.*

Fourth, if all of the Postal Service’s institutional costs had to be assigned to either Market Dominant or Competitive products (which, for the reasons discussed above and in Section IV.B.2., *supra*, relies on both a flawed interpretation of the statute and an arbitrary method of cost allocation that would produce unreasonable results similar to fully distributed costing), doing so based on attributable cost shares would be particularly problematic, because there is no evidence that mailpieces with higher attributable cost are more responsible for institutional costs than mailpieces with lower attributable cost.

Without evidence to the contrary, the least unreasonable option would be to allocate the Postal Service’s institutional costs based on volume shares. While the Commission maintains that the primary focus of the appropriate share provision is to protect competition rather than to ensure a particular level of institutional cost coverage, it is noteworthy that if it were to allocate all institutional costs to Market Dominant and Competitive products by assigning the same amount of institutional cost to every mailpiece, an even lesser amount of costs would be assigned to Competitive products than the amount produced by the Commission’s dynamic formula-based approach (*i.e.*, approximately 5.6 percent under the volume-based allocation compared to 9.1 percent

under the Commission's dynamic formula-based approach in FY 2021). As Pitney Bowes and the Public Representative observe, no evidence in the record indicates that UPS's proposed use of attributable cost shares would be more economically rigorous than the Commission's dynamic formula-based approach. See PR Reply Comments at 10; see *also* Pitney Bowes Reply Comments at 11-12.

For these reasons, the Commission again declines to adopt UPS's proposal to set the appropriate share level based on Competitive products' share of the Postal Service's overall attributable costs.

B. Reference to Market Dominant Contribution

1. Introduction

In response to Order No. 6043, UPS introduces a new alternative proposal to set the appropriate share by reference to the Postal Service's Market Dominant product contribution to institutional costs. UPS Comments at 48-49. ASL, Pitney Bowes, the Postal Service, and the Public Representative oppose UPS's Market Dominant contribution approach.²⁶¹ ASL's opposition relies (in part) on analysis performed by Dr. Panzar. See ASL Reply Comments at 1; Panzar Reply Decl. at 2, 6-8, 17.

2. Comments

UPS suggests that, instead of its formula-based approach, the Commission could require Competitive products to cover "whatever share of institutional costs are *not* covered" by Market Dominant products. UPS Comments at 48. Similar, to its attributable cost share proposal, UPS states that its approach does not constitute fully distributed costing, even though it would also allocate 100 percent of institutional costs

²⁶¹ See ASL Reply Comments at 21-22; Pitney Bowes Reply Comments at 11-13; Postal Service Reply Comments at 60-66; PR Reply Comments at 13.

between Market Dominant and Competitive products. UPS Comments at 48-49. UPS presents a table that depicts changes in Market Dominant product contribution since FY 2007 and what their proposed alternative would have looked like in terms of Competitive product contribution. *Id.* at 49, Table 1.

As a threshold matter, the Public Representative rejects UPS's Market Dominant contribution approach, noting that the PAEA does not mandate the full recovery of institutional costs. PR Reply Comments at 13. The Postal Service observes that 39 U.S.C. § 3622(b)(9) does not indicate what the size of the appropriate share should be because that provision relates to the regulation of Market Dominant products. Postal Service Reply Comments at 62. It contends that UPS uses its "flawed view" of 39 U.S.C. § 3622(b)(9) as a "springboard" to propose that Competitive products' appropriate share be set at 100 percent minus the contribution of Market Dominant products. *Id.* at 63.

The Postal Service maintains that UPS's Market Dominant contribution approach ignores the language of 39 U.S.C. § 3633(b). It states that the amount of institutional costs not covered by Market Dominant products "has nothing to do with costs that are uniquely or disproportionately associated with Competitive products." *Id.* Similarly, Pitney Bowes and Dr. Panzar observe that UPS's Market Dominant contribution approach fails to consider whether the costs left over after Market Dominant product contribution are uniquely or disproportionately associated with Competitive products and therefore is contrary to 39 U.S.C. § 3633(b). Pitney Bowes Reply Comments at 1; Panzar Reply Decl. at 7-8.

The Postal Service further maintains that UPS's Market Dominant contribution approach is at odds with the "prevailing competitive conditions in the market" language of 39 U.S.C. § 3633(b). Postal Service Reply Comments at 63. The Postal Service states that "[t]he Commission cannot take account of how Competitive products are faring in the broader package delivery market, as it is required to do under the statute, if

the appropriate share is already determined simply by default as a function of exogenous trends in the finances of Market Dominant products” *Id.*

ASL, Pitney Bowes, and Dr. Panzar assert that setting the appropriate share to cover the share of institutional costs that are not covered by Market Dominant products would arbitrarily allocate institutional costs like fully distributed costing and would be economically unsound. ASL Reply Comments at 22; Pitney Bowes Reply Comments at 11-13; Panzar Reply Decl. at 7. Dr. Panzar elaborates that UPS’s Market Dominant contribution approach is “inherently arbitrary and would distort rather than promote fair competition,” as it would force the Postal Service to set prices well above incremental costs regardless of rival behavior. Panzar Reply Decl. at 7.

The Public Representative asserts UPS’s Market Dominant contribution approach “suffers from several fatal defects.” PR Reply Comments at 13. He adds that “UPS’s method is not economically sound, it is simply an arithmetic allocation designed to produce 100 percent [of institutional costs] on paper.” *Id.*

The Postal Service contends that UPS’s Market Dominant contribution approach relies upon the incorrect assumption that Competitive products or the appropriate share itself are to blame for the Postal Service’s failure to cover all its institutional costs. Postal Service Reply Comments at 61-62. Instead, the Postal Service adduces that the facts indicate “that the true root of the overall shortfall is the Market Dominant shortfall” *Id.* at 62. The Postal Service asserts that if UPS’s proposal were implemented and Market Dominant contribution continues to fall, then Competitive products’ appropriate share would automatically increase and “it would only be a matter of time before Competitive products are priced out of the market and the Competitive contribution would itself decline.” *Id.* at 64. Finally, the Postal Service contends that UPS’s proposal does not have a common-sense result as evidenced by the abrupt fluctuations in Competitive product contribution that would have occurred should UPS’s proposal been in place. *Id.* at 65; see also UPS Comments at 49, Table 1. It further contends that

UPS's proposal would do nothing to remedy shortfalls in Market Dominant product contribution. Postal Service Reply Comments at 65-66.

Dr. Panzar explains that "[a] little algebra shows that this is equivalent to requiring that the Commission reimpose a break-even constraint on the Postal Service," which was abandoned by the enactment of the PAEA. Panzar Reply Decl. at 7.

3. Commission Analysis

UPS proposes setting Competitive products' appropriate share by reference to the Postal Service's Market Dominant product contribution to institutional costs. The Commission concludes that the UPS's Market Dominant contribution approach has many of the same defects as its proposal to allocate institutional cost based on attributable cost shares.²⁶² UPS's Market Dominant contribution approach relies on both a flawed interpretation of the statute²⁶³ and an arbitrary method of cost allocation that would produce unreasonable results similar to fully distributed costing. ASL Reply Comments at 22; Pitney Bowes Reply Comments at 11-13. The arbitrary assignment of shares of institutional costs to Competitive products is functionally identical to the economic concept of fully distributed costing. See Order No. 6043 at 85-86; Pitney Bowes Reply Comments at 12-13. Although UPS's Market Dominant contribution approach does not allocate institutional costs to specific products, it does allocate all postal costs to either Market Dominant products or Competitive products as a group, and thereby increases the minimum prices the Postal Service would be able to charge

²⁶² See ASL Reply Comments at 21-22; Pitney Bowes Reply Comments at 11-13; Postal Service Reply Comments at 52-66; PR Reply Comments at 9-13.

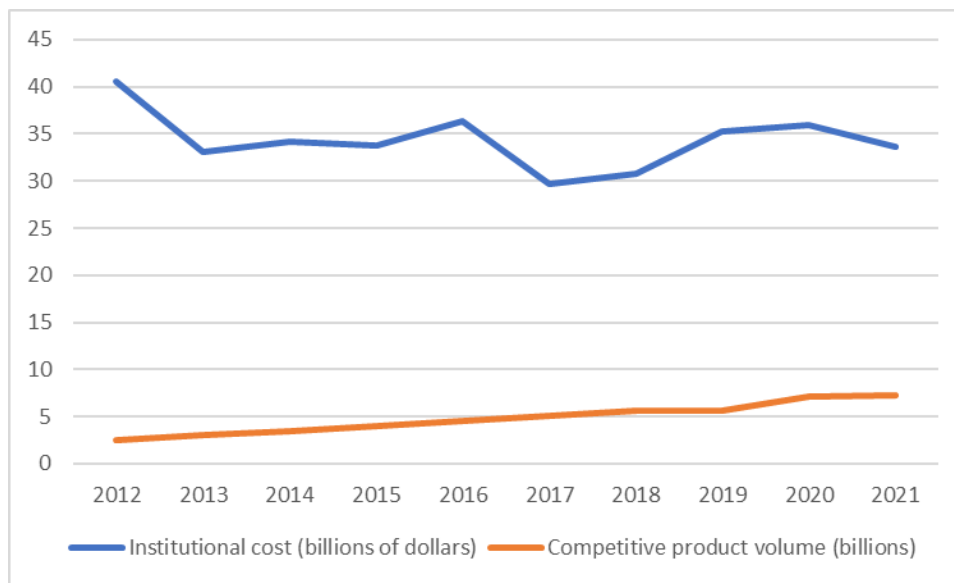
²⁶³ See Section VIII.A.3., *supra*. As stated above, 39 U.S.C. § 3622(b)(9) does not apply or require any regulatory action with respect to the Competitive product ratemaking system and UPS's preferred interpretation would conflict with the Commission's express authority to eliminate the appropriate share under 39 U.S.C. § 3633(b). Additionally, the Postal Service's Market Dominant contribution does not account for the Postal Service's market power, the size of the overall parcel delivery market, or any other "prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products." 39 U.S.C. § 3633(b).

for its Competitive products. See Order No. 6043 at 85-86; Pitney Bowes Reply Comments at 13. Thus, the Commission finds that adopting UPS's proposal would hinder the Postal Service's ability to price its Competitive products based on demand characteristics and effectively compete with its competitors. See Postal Service Reply Comments at 64-65; Panzar Reply Decl. at 7. For these reasons alone, the Commission cannot adopt UPS's Market Dominant contribution approach. Additional defects, specific to UPS's Market Dominant contribution approach are discussed below.

First, UPS's Market Dominant contribution approach lacks a basis in sound economic principles. By way of background, institutional costs are residual costs or the costs that remain after all reliably identifiable, causally related product-level and group-level costs have been attributed. Order No. 6043 at 72.

Below, Figure VIII-4 compares changes in Competitive product volume and changes in institutional cost since FY 2012.

Figure VIII-4
Competitive Product Volume and Postal Service Institutional Cost,
FY 2012–FY 2021



Source: FY 2012 ACD; FY 2013 ACD; Library Reference PRC-LR-ACR2014/1; Library Reference PRC-LR-ACR2015/1; Library Reference PRC-LR-ACR2016/1; Library Reference PRC-LR-ACR2017-1; Library Reference PRC-LR-ACR2018-1; Library Reference USPS-FY19-1; Library Reference PRC-LR-ACR2020-1; Library Reference PRC-LR-ACR2021-1.

As Figure VIII-4 shows, the Postal Service's total institutional costs have fluctuated over time, whereas its Competitive product business has grown steadily in the same time frame. This is because changes in Competitive product volume are not related to changes in institutional costs. Similarly, changes in the amount of institutional costs covered by Market Dominant products are not related to changes in Competitive product volume, and thus the amount of institutional costs not covered by Market Dominant products is not related to Competitive products' appropriate share of institutional costs. In fact, two classes of mail and several products within Market Dominant products do not contribute any amount to the Postal Service's institutional costs. In FY 2021, these classes and products made up more than 10 percent of Market Dominant product volume. Library Reference PRC-LR-ACR2021-1. Under

UPS's Market Dominant contribution approach, the Postal Service's Competitive products would be required to make up for the shortfall from these Market Dominant classes and products, which operate in a market existing completely outside of the competitive marketplace and with their ability to generate revenue constrained by price cap regulation. See 39 U.S.C. § 3622. The Commission asserts that such a result is economically unsound and would put an undue burden on Competitive products not intended by the PAEA.

Second, under UPS's Market Dominant contribution approach, Competitive products' appropriate share is entirely dependent on Market Dominant products' ability to contribute to the Postal Service's institutional costs. The approach does not account for recent trends in Market Dominant products, namely the considerable decline in Market Dominant mail volume. If Market Dominant mail volume continues to decline and its institutional cost contribution continues to decrease, Competitive products would be responsible for an ever-increasing appropriate share of institutional costs, regardless of competitive market conditions such as market expansion or contraction. The Commission finds that it would contravene 39 U.S.C. § 3633(b) and would be inappropriate to allocate the Postal Service's institutional costs in a manner that does not give any consideration to the market conditions affecting the Postal Service's Competitive products. This is because additional losses in Market Dominant volume could easily drive up the Competitive products' appropriate share, which would require the Postal Service to increase Competitive product prices. These price increases would not be based on competitive market signals; instead, such increases would be based (incorrectly) on changes in a separate and unrelated marketplace. See Postal Service Reply Comments at 63-64. Such a result could lead to Competitive products' failure to maximize contribution to institutional costs. Put simply, based solely on the performance of Market Dominant products, the Postal Service could be forced to set Competitive product prices that would result in losing profitable Competitive product volume and decrease institutional cost contribution.

Third, adopting UPS's Market Dominant contribution approach would be the functional equivalent of reimposing the breakeven requirement in contravention of the PAEA. Dr. Panzar accurately highlights the similarities between UPS's Market Dominant contribution approach and the PRA-style cost-of-service model of regulation that was eliminated with the enactment of the PAEA. Panzar Reply Decl. at 7-8. Using simple algebra, Dr. Panzar demonstrates that UPS's proposed methodology is "equivalent to the requirement that the Postal Service at least break-even" *Id.* at 7. Under the PRA, the assignment of the Postal Service's institutional costs was designed to ensure that each subclass or type of mail made a reasonable contribution to its institutional cost, yielding prices that were fair and equitable and subsidy-free. Order No. 6043 at 16. Under the PAEA, the PRA cost-of-service system was abolished. *Id.* at 22. The PAEA's approach to pricing addresses the issues of price levels and subsidies differently than the approach of the PRA. Prices for Competitive products must satisfy criteria that prevent the possibility of subsidization by Market Dominant products. See 39 U.S.C. § 3633(a); see *also* Order No. 6043 at 22-25. In Order No. 26, the Commission explained the significance of the difference between the two approaches governing pricing of Competitive products as follows:

The "appropriate share" required by the PAEA is not synonymous with "reasonably assignable" required by PRA section 3622(b)(3) Moreover, the resulting rate levels represent significantly different things. Under the PRA, rate levels equate with maximum rates for the subclass or type of mail, as rates are not designed to generate a surplus. In contrast, under the PAEA, the concept of rate levels for competitive products largely disappears, with the Postal Service given the flexibility to price competitive products however it wishes, provided its rates satisfy the statutory standards of lawfulness. Appropriate share is a floor for all competitive products, but the hope (and expectation) is that competitive products will generate contributions in excess of the floor. Thus, it is unlike reasonably assignable in two other respects: it applies to competitive products collectively, not to subclasses or services individually; and it represents a minimum (not maximum) contribution level, serving as a threshold for compliance with section 3633(a)(3).

Order No. 26 ¶ 3056.

Thus, adopting UPS's Market Dominant contribution approach would eliminate much of the pricing flexibility afforded to the Postal Service and its Competitive products under the PAEA. Under UPS's Market Dominant contribution approach, Competitive products' appropriate share would be comparable to the Commission setting a maximum price level, something the PAEA sought to eliminate in favor of granting the Postal Service pricing flexibility for its Competitive products. See Order No. 6043 at 13-14, 24, 43, 47. The Commission has described the risks of setting the appropriate share too high—distorting the occurrence of fair competition in the market for competitive postal services—by conferring an unfair competitive advantage on competitors of the Postal Service that could harm consumers and the Postal Service's ability to compete. *Id.* at 61.

For these reasons, the Commission declines to adopt UPS's Market Dominant contribution approach.

C. Stand-Alone Market Dominant Costs

1. Introduction

In response to Order No. 6043, UPS introduces a new alternative proposal to set the appropriate share by analyzing stand-alone costs of the Postal Service's Market Dominant business. UPS Comments at 50-57. ASL, Pitney Bowes, the Postal Service, and the Public Representative oppose UPS's stand-alone cost approach.²⁶⁴ ASL's opposition relies (in part) on analysis performed by Dr. Panzar. See ASL Reply Comments at 1 (citing Panzar Reply Decl.).

²⁶⁴ See ASL Reply Comments at 22-23; Pitney Bowes Reply Comments at 13-14; Postal Service Reply Comments at 66-70; PR Reply Comments at 14.

2. Comments

UPS claims that the Commission could model the stand-alone costs of the Postal Service's Market Dominant business and determine "what the Postal Service's business would look like in the absence of competitive products." UPS Comments at 50. UPS contends that the Postal Service would then be able to isolate "via simple subtraction" costs uniquely and disproportionately associated with Competitive products and use that amount to "inform the appropriate share percentage." *Id.* UPS argues that a stand-alone cost methodology would allow the Commission to determine which portion of institutional costs are unattributed inframarginal costs and would avoid cross-subsidization. *Id.* UPS contends that such a model would reveal aspects of the Postal Service's operations that result from Competitive products, such as the ability to quantify the "'peak season' crunch," operational costs, investments in its package delivery business, and larger postal vehicles—costs UPS claims are driven by Competitive products. *Id.* at 50-54. UPS adds that the Surface Transportation Board (STB) uses this method to assess the reasonableness of prices charged by regulated entities. *See id.* at 50-51.

As a threshold matter, Pitney Bowes contends that UPS's stand-alone cost approach is legally deficient because for purposes of the 39 U.S.C. § 3633(b) review, costs must be "uniquely or disproportionately associated" rather than merely associated. Pitney Bowes Reply Comments at 14. Dr. Panzar states that UPS's stand-alone approach constitutes "an alternative approach to determining whether or not the Postal Service's Competitive products are cross-subsidized: i.e., an alternative approach for measuring the incremental costs of the Postal Service's Competitive products." Panzar Reply Decl. at 9. He asserts that UPS's approach "would be more appropriately addressed" in discussing the cross-subsidy requirements of 39 U.S.C. § 3633(a) rather than discussing the review of the appropriate share under 39 U.S.C. § 3633(b). *Id.*

The Postal Service disagrees with UPS's assertion that, by subtracting Market Dominant stand-alone costs from total costs, uniquely or disproportionately associated costs are isolated. Postal Service Reply Comments at 67. The Postal Service states that such an exercise only isolates Competitive products' incremental costs. *Id.* Pitney Bowes asserts that UPS's stand-alone cost proposal fails on practical, legal, and theoretical grounds. Pitney Bowes Reply Comments at 13. ASL asserts that UPS's suggestion that modeling the stand-alone costs of the Market Dominant business "could be done simply is unserious." ASL Reply Comments at 22.

Dr. Panzar explains that the existing "top down" approach used by the Postal Service and approved by the Commission starts with observable Postal Service total costs and volumes and uses an *activity-based costing* methodology to estimate the costs that would be *avoided* if the Postal Service's Competitive product volumes were eliminated." Panzar Reply Decl. at 10 (emphasis in original). By contrast, he states that the "indirect, 'bottom up'" stand-alone approach proposed by UPS "would be a 'greenfields' approach." *Id.*

Dr. Panzar adds that "[i]n theory" whether to calculate Competitive product incremental costs directly or indirectly (by calculating stand-alone Market Dominant product costs and subtracting that from the Postal Service's total costs) is "a matter of indifference." *Id.* at 9 (emphasis in original). However, he elaborates that "the theoretical duality" is predicated upon the use of long-run costs of a hypothetically efficient enterprise. *Id.* at 9-10. He states that in practice, "the cost data available do not meet [that] idealized standard[.]" in part because UPS's approach is not measuring costs of "the *same* enterprise."²⁶⁵ As a result, he maintains the Commission's use of

²⁶⁵ *Id.* (emphasis added). UPS's stand-alone approach would use the *existing* total accrued costs of the Postal Service and subtract "*greenfield*" stand-alone Market Dominant product costs, which Dr. Panzar maintains is an "apples to oranges" comparison because the approach is not measuring costs of the *same* enterprise, but of two different enterprises. *Id.* at 13 (emphasis added).

incremental costs “is both more practical and theoretically appropriate than the indirect approach proposed by UPS.” *Id.* at 10.

Mainly, Dr. Panzar contends that the practical problem with UPS’s stand-alone approach compared to the existing use of incremental costs is the “disparity in how much is being asked of the estimation process.” *Id.* Because the “indirect, ‘bottom up’” stand-alone approach proposed by UPS “would be a ‘greenfields’ approach[.]” Dr. Panzar explains that UPS’s stand-alone approach would require the analyst to “go back to the drawing board” to design “an efficient network to serve only the Market Dominant volumes of the Postal Service *and* estimate the costs of operating such a network.” *Id.* (emphasis in original). Furthermore, he notes that “[b]ecause the Postal Service’s Competitive products represent a relatively small percentage of its total volume, the magnitude of the stand-alone cost task is far greater than that required for the incremental cost analysis.” *Id.* at 10-11.

Pitney Bowes states that UPS’s “notion that the modeling of a hypothetical, multi-billion dollar, standalone market dominant postal delivery business, involving countless counterfactual assumptions, is a simple exercise is not credible.” Pitney Bowes Reply Comments at 13-14. Pitney Bowes adds that there is no reason to invest time and expense into attempting to model Market Dominant products’ stand-alone business when the aggregate incremental cost calculated under 39 U.S.C. § 3633(a)(1) should generate the same result in the other direction. *Id.* at 14. Similarly, the Postal Service also maintains that calculating stand-alone costs is “an expensive and time-consuming process that requires constructing an operating plan for a hypothetical entity and then attempting to further construct costs for that entity[.]” Postal Service Reply Comments at 68.

ASL states that UPS’s stand-alone approach is “unworkable” and “plagued with obstacles in obtaining an estimate that is theoretically correct and sufficiently reliable for regulatory purposes.” ASL Reply Comments at 22-23. ASL asserts that UPS’s stand-

alone approach is “unnecessary” observing that, by definition, the difference between total costs and total costs without account for Competitive products is the incremental costs of those products, which is already calculated, and no cross-subsidization ensured, under 39 U.S.C. § 3633(a)(1). *Id.* at 22.

The Public Representative also rejects UPS’s stand-alone approach because a portion of institutional costs, those caused by Market Dominant and Competitive products simultaneously, cannot be separated. PR Reply Comments at 14. He states that UPS is silent on several relevant topics including how stand-alone cost modeling would account for the intricacies of simultaneous handling of Market Dominant and Competitive products, the impact of the loss of scope economies after separation, and the assumptions that would be made regarding the efficiency of stand-alone costs. *Id.*

ASL further observes that UPS acknowledges that stand-alone modeling used by the STB has proven “complex[] and expens[ive].” ASL Reply Comments at 23 (quoting UPS Comments at 51 n.98). With respect to the STB’s use of the stand-alone approach in the railroad industry, Dr. Panzar explains that its use is “not without significant controversy” and requires significant expense to model stand-alone costs. Panzar Reply Decl. at 11. Moreover, he explains that the STB uses stand-alone costs analyses “to establish *price ceilings* for rates that can be charged to so-called ‘captive shippers.’” *Id.* (emphasis in original).

3. Commission Analysis

UPS proposes setting Competitive products’ appropriate share by analyzing stand-alone costs of the Postal Service’s Market Dominant business. The Commission concludes that UPS’s stand-alone approach has many of the same defects as its proposals to allocate institutional cost based on attributable cost shares or by reference to Market Dominant contribution.

UPS's stand-alone approach relies on both a flawed interpretation of the statute²⁶⁶ and an arbitrary method of cost allocation that would produce unreasonable results like fully distributed costing. Notwithstanding UPS's claims to the contrary, UPS's stand-alone approach arbitrarily allocates all the Postal Service's costs to either Market Dominant products or Competitive products, even those costs that cannot be linked to either grouping in a non-arbitrary way. For these reasons alone, the Commission cannot adopt UPS's stand-alone approach. Additional defects, specific to UPS's stand-alone approach are discussed below.

First, the Commission acknowledges that, to some extent, the methodology proposed by UPS *appears* to be reasonable on its face. That is, if the cost of the Postal Service's entire Market Dominant business could be quantified, it follows that any other cost the Postal Service incurs would be due to its Competitive product business. However, below the surface, UPS's stand-alone approach is problematic. Stand-alone cost modeling assumes that "stand-alone, incremental, and total cost measures in the equation are measured or estimated with respect to the *same* enterprise." Panzar Reply Decl. at 12 (emphasis in original). However, UPS's stand-alone approach does not base cost allocations on the Postal Service's operations as they exist today. See Panzar Reply Decl. at 10-14; UPS Comments at 51. Instead, under UPS's stand-alone approach, the costs allocated to the Postal Service's Market Dominant products would be only those of an *idealized* Market Dominant business. See Panzar Reply Decl. at 12-14; UPS Comments at 51. UPS's calculations rely upon a hypothetically efficient

²⁶⁶ See Sections VIII.A.3., VIII.B.3., *supra*. As stated above, 39 U.S.C. § 3622(b)(9) does not apply or require any regulatory action with respect to the Competitive product ratemaking system and UPS's preferred interpretation would conflict with the Commission's express authority to eliminate the appropriate share under 39 U.S.C. § 3633(b). Additionally, UPS's stand-alone approach would be based solely on cost estimates, which does not account for the Postal Service's market power, the size of the overall parcel delivery market, or any other "prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products." 39 U.S.C. § 3633(b).

Market Dominant enterprise that does not exist. See Panzar Reply Decl. at 12-14; UPS Comments at 51.

The Commission notes that such an exercise is even more problematic because the costs that remain would be made up of Competitive product costs (which UPS's stand-alone approach intends) *as well as* costs incurred by the Postal Service's Market Dominant products that are present under the current system (which UPS's stand-alone approach does not intend). This is because, in attempting to capture the costs of a hypothetically efficient enterprise, costs that occur due to inefficiencies in the current system by Market Dominant products would be left out. Thus, UPS's stand-alone approach would not isolate costs uniquely or disproportionately associated with Competitive products as UPS claims. See UPS Comments at 50. Instead, UPS's stand-alone approach would go further to capture a portion of costs that occur under the current system and are caused by Market Dominant products.

Second, the modeling of stand-alone Market Dominant costs to determine the cost of the Postal Service's Competitive product business would be unreasonably burdensome. The best estimate of costs that are uniquely or disproportionately associated with Competitive products is their total incremental cost—the existing Commission-approved methodology.²⁶⁷ Incremental costs are the costs that would disappear if the Postal Service's Competitive business was discontinued. Order No. 6043 at 25. And, as Dr. Panzar explains, “[i]n *theory*, it is a matter of indifference whether one calculates the incremental costs of Competitive products directly or calculates the stand-alone costs of Market Dominant products and subtracts it from the (observed) total costs of the Postal Service.” Panzar Reply Decl. at 9 (emphasis in original). UPS's stand-alone approach is fundamentally unnecessary because the Commission already estimates the incremental costs of the Postal Service's

²⁶⁷ Pitney Bowes Reply Comments at 14; ASL Reply Comments at 22; Postal Service Reply Comments at 67; Panzar Reply Decl. at 10.

Competitive products directly, to test for cross-subsidization pursuant to 39 U.S.C. § 3633(a)(1). See Order No. 6043 at 26.

With respect to burden, although the Commission is unable to evaluate UPS's stand-alone approach in detail because UPS did not elaborate on how it would separate the Postal Service's cost function into two independent parts, and what other assumptions it would make in the development of the stand-alone cost of Market Dominant products (see PR Reply Comments at 14), the Commission can consider what the estimation process for stand-alone Market Dominant costs would require from a theoretical perspective. Notwithstanding the simplistic appearance of UPS's stand-alone approach, it is prohibitively complex in practice. As Dr. Panzar observes, when choosing an appropriate approach, "how much is being asked of the estimation process" is an important consideration. Panzar Reply Decl. at 10. The Commission agrees with Dr. Panzar that "[b]ecause the Postal Service's Competitive products represent a relatively small percentage of its total volume, the magnitude of the stand-alone cost task is far greater than that required for the incremental cost analysis." *Id.* at 10-11. Dr. Panzar correctly observes that "[c]alculating the stand-alone costs of Market Dominant products requires a *de novo* recreation of most of the Postal Service network, while calculating the incremental costs of Competitive products involve[s] only quantifying relatively small cost changes from current output levels using well established methodologies." *Id.* at 11.

Overall, duplicating the existing direct methodology to model the cost of the Postal Service's Competitive product business (but doing so in reverse and using an unreliable methodology) would be time-consuming, expensive, and unhelpful in analyzing costs. Thus, the Commission concludes that the time and expense needed to develop UPS's stand-alone approach would not be justified given that the cost of the

Postal Service's Competitive product business is already calculated using the incremental cost test pursuant to 39 U.S.C. § 3633(a)(1).²⁶⁸

Third, to bolster its claim that its stand-alone approach is reasonable, UPS references that the STB implements a test based on stand-alone costs to assess the reasonableness of prices charged by regulated entities in the railroad industry. See UPS Comments at 50-51. UPS appears to imply that the stand-alone approach would be straightforward and similarly applicable to the Commission's review pursuant to 39 U.S.C. § 3633(b). However, the STB uses the stand-alone test to determine a maximum price, *i.e.*, a ceiling on prices charged by railroads to captive shippers. See Panzar Reply Decl. at 11; Postal Service Reply Comments at 68-70. By contrast, the appropriate share represents a minimum (not a maximum) contribution level. Order No. 6043 at 47. Thus, adopting a stand-alone approach would be inconsistent with the Commission's review pursuant to 39 U.S.C. § 3633(b). Moreover, stand-alone modeling used by the STB has proven to be "complex[] and expens[ive]," which further underscores that adapting such an approach to the postal sector would be prohibitively burdensome and ultimately unworkable (setting aside that doing so would be inappropriate for other reasons).²⁶⁹

D. Regression-Based Approach

1. Introduction

In response to Order No. 6043, UPS introduces a new alternative proposal, which relies on a regression to estimate costs "uniquely or disproportionately associated" with Competitive products within the Postal Service's institutional costs.

²⁶⁸ See ASL Reply Comments at 22-23; Panzar Reply Decl. at 9-14; Pitney Bowes Reply Comments at 13-14; Postal Service Reply Comments at 66-70.

²⁶⁹ ASL Reply Comments at 23 (quoting UPS Comments at 51 n.98). See Postal Reply Service Comments at 69-70.

UPS Comments at 57-63. UPS submits a non-public technical appendix regarding its regression-based approach developed by external consultants.²⁷⁰ ASL, Pitney Bowes, the Postal Service, and the Public Representative oppose UPS's regression-based approach.²⁷¹ The Postal Service's opposition relies (in part) on analysis performed by George Washington University Professor of Economics, Dr. Michael D. Bradley. See Postal Service Reply Comments at 72-73; *see also generally* Bradley Report.

2. Comments

UPS claims that the Commission could use a regression-based approach to identify costs uniquely or disproportionately associated with Competitive products and use that information to inform its appropriate share determination. UPS Comments at 57. It states that its external consultants developed a regression-based approach to identify costs uniquely or disproportionately associated with Competitive products, using data from ACDs and other monthly and quarterly reports involving costs, volumes, and mail mix data. *Id.* UPS notes that the data cover 8 years and capture Market Dominant product volume decline and seasonal variation in Market Dominant and Competitive product volumes. *Id.* UPS states that several adjustments are made to compile monthly data that are otherwise presented quarterly or annually. *Id.* at 58-59.

UPS's regression-based approach "begins by defining the residual costs that will serve as the dependent variable." *Id.* at 58. To accomplish this, UPS's regression-based approach computes the monthly volume-variable cost for a cost component by multiplying the cost component's annual variability by its monthly accrued costs. *Id.* That amount is then deducted from the cost component's total accrued costs, and the

²⁷⁰ Library Reference UPS-LR-RM2022-2/NP1. UPS filed this material under seal and sought non-public treatment. Notice of Filing of Library Reference UPS-LR-RM2022-2/NP1 and Application for Nonpublic Treatment, February 25, 2022.

²⁷¹ See ASL Reply Comments at 23-26; Pitney Bowes Reply Comments at 13-14; Postal Service Reply Comments at 70-73; PR Reply Comments at 14.

remainder represents “non-volume variable” costs of the cost component which “forms the residual cost measure.” *Id.* UPS notes that for this dependent variable, “cost category wide variables” from FY 2021 are applied and are adjusted by inflation. *Id.* at 58-59.

Next, UPS states that to measure the association of these residual costs with products, “volume measures for each type of product must be calculated.” *Id.* at 59. Product-level volumes are not calculated quarterly. Thus, UPS explains that “a measure of weighted volume that corresponds to differences in the amount of cost driver units that are needed to move the average piece of mail of that type” is used and is based upon the constant elasticity model approved by the Commission. *Id.* UPS further explains that cost driver units per piece are multiplied by piece counts and then summed into three categories: domestic Competitive products, domestic Market Dominant products, and international mail. *Id.* It notes that although the resulting monthly sums “constitute the key explanatory variables of interest[,]” the residual costs “can also vary for reasons other than variation in mail volumes.” *Id.* at 59-60. Thus, to “account for such effects, the analysis incorporates a rich set of control variables,” which UPS states are outlined in detail in its Technical Appendix. *Id.* at 60; see *id.* Technical App’x.

According to UPS, calculations are needed to convert these relationships into dollar figures that identify costs uniquely or disproportionately associated with Competitive products. UPS Comments at 61. First, coefficients for Competitive products are multiplied by the volume-variable costs in the most recent fiscal year, which yields a measure of costs disproportionately associated with Competitive products from the previously calculated residual costs. *Id.* Next, the inframarginal costs associated with Competitive products are deducted from the calculated disproportionately associated costs. *Id.* UPS claims that the resulting amounts are “not only disproportionately, but rather, *completely* associated” with Competitive products.

Id. (emphasis in original). Under UPS's proposal, the Commission would "assign" \$3.8 billion of "associated" costs to Competitive products via the appropriate share but would then need to "assign" an "appropriate share" of the remaining \$27.9 billion in costs identified by the regression as associated with neither Market Dominant products nor Competitive products, *i.e.*, common costs. *Id.* at 62. UPS contends that, for there to be a level playing field, and for the Postal Service to be financially stable, Competitive products must "cover an appropriate share of these costs." *Id.* at 63.

As a threshold matter, the Postal Service contends that UPS's regression-based approach is not consistent with the language of 39 U.S.C. § 3633(b), which it uses "as a convenient excuse in its bid to invoke methodologies utilizing extended inferences of causation that are insufficiently reliable to meet the required standard for attribution." Postal Service Reply Comments at 71-72.

ASL asserts that UPS's regression-based approach relies on an incorrect assumption and "contrary to UPS's position, there is no correlation between rising package volumes and institutional costs." ASL Reply Comments at 24. Similarly, Pitney Bowes observes that a relationship between Competitive product volume and institutional costs is not supported by the data. Pitney Bowes Reply Comments at 14-15.

The Postal Service maintains that UPS's regression-based approach does not measure what it intends to measure, which is a relationship between non-volume-variable costs and volume. Postal Service Reply Comments at 72-73. Dr. Bradley elaborates that UPS's regression-based approach "does not actually investigate the variation in non-volume-variable costs and fails to estimate a statistically reliable or economically meaningful relationship" between costs and products. Bradley Report at 2. Dr. Bradley criticizes how UPS constructs its regression data sets, namely the four monthly non-volume-variable cost series for the four large groupings of costs UPS refers to as "cost categories." *Id.* at 7-9. He demonstrates that under UPS's

regression-based approach, what appears to be variation in non-volume-variable cost is just the variation in accrued costs. *Id.* In addition, he evaluates UPS's regressions as time series variability equations, computing variabilities for the four cost categories. *Id.* at 10-11. Dr. Bradley discusses the "very unusual pattern" of the resulting variabilities and contends that the variabilities are at odds with operational experience. *Id.* at 11.

ASL explains that UPS's attempt to multiply monthly volumes by annual unit costs to create monthly workload-weighted volume figures is inappropriate and was previously rejected by the Commission in Docket No. RM2020-9 as improper. ASL Reply Comments at 24. ASL cites to UPS's assumption that inflation-adjusted unit costs "did not vary at all month-to-month or year-to-year" in the last 8 years and illustrates that such an assumption is incorrect. *Id.* at 25-26, Table 1. ASL and Pitney Bowes assert that the Commission should reject UPS's regression-based approach as "unreliable" for the same reasons it rejected UPS's proposals in Docket Nos. RM2016-2 and RM2020-9. See *id.* at 23; Pitney Bowes Reply Comments at 14-15.

The Public Representative asserts that UPS's regression-based approach leads to ambiguous and unconvincing results because it disaggregates annual data into monthly data explaining only the variation in monthly accrued costs, and it heavily relies on the untested "implicit assumption that all year-specific slopes of the explanatory variables are equal" PR Reply Comments at 14. He also notes that, generally, UPS uses the same variability used to causally attribute costs "to argue for association between a different set of costs and products[,] ones that are already captured by the initial variability estimate. *Id.* at 15.

The Postal Service argues that UPS's regression-based approach is evidence that "UPS mistakenly views the entire appropriate share review process, rather than as a pricing exercise for the purpose of determining appropriate shares of institutional costs, as merely an opportunity for a do-over of the costing function." Postal Service Reply Comments at 70. It further argues that UPS's regression-based approach

“leaves UPS with nowhere to hide in response to the valid observation that its intent is to create a separate and distinct third tier of ‘associated’ costs” that are neither attributable nor institutional. *Id.* ASL characterizes UPS’s regression-based approach as “a mash-up of two UPS proposals the Commission previously considered and rejected as unreliable.” ASL Reply Comments at 4. More specifically, ASL describes UPS’s regression-based approach as a “warmed-over version” of UPS’s proposals from Docket Nos. RM2016-2 and RM2020-9,²⁷² which attempted to shift costs from the Postal Service’s institutional costs to Competitive products’ attributable costs and was rejected by the Commission. ASL Reply Comments at 23-24.

Finally, ASL notes that UPS’s regression-based approach produces a cost estimate not all that dissimilar from the Commission’s dynamic formula-based approach (\$3.8 billion versus \$3.1 billion) and reiterates that Competitive products’ most recent institutional cost contribution “significantly exceeds” both of those values (\$13.2 billion in FY 2021). *Id.* at 26.

3. Commission Analysis

UPS claims its regression-based approach estimates the relationship between Competitive, domestic Market Dominant, and international volumes and non-volume-variable costs over an 8-year period, which it asserts can be used to identify costs that are disproportionately associated with Competitive products. UPS Comments at 57-63. The Commission concludes that UPS’s regression-based approach has many of the same defects as its proposals to allocate institutional cost based on attributable cost shares or by reference to Market Dominant contribution. UPS’s regression-based

²⁷² See Order No. 6048.

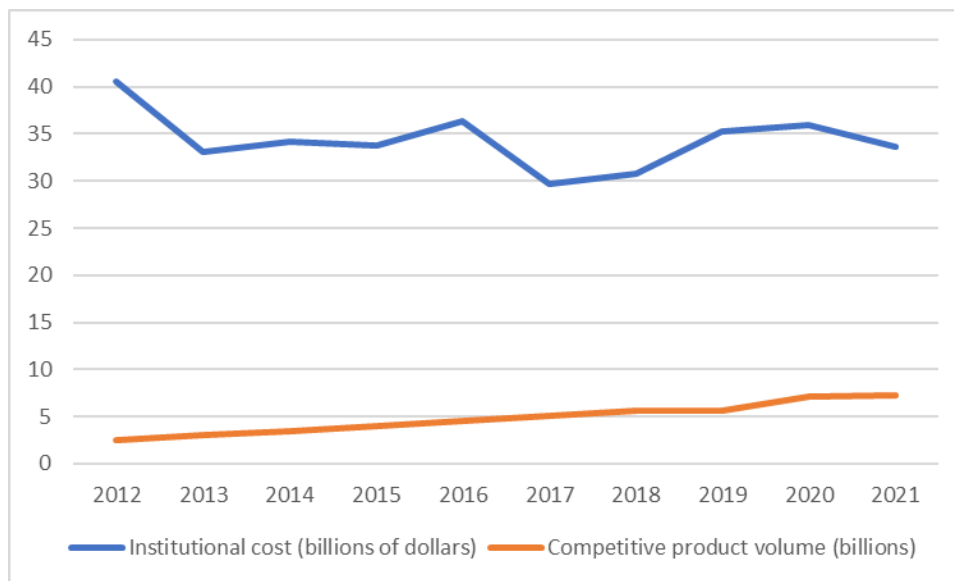
approach relies on both a flawed interpretation of the statute²⁷³ and an arbitrary method of cost allocation that would produce unreasonable results like fully distributed costing. Notwithstanding UPS's claims to the contrary, UPS's regression-based approach arbitrarily allocates all the Postal Service's costs to either Market Dominant products or Competitive products,²⁷⁴ even those costs that cannot be linked to either grouping in a non-arbitrary way. The Commission has consistently held that regardless of the cost allocation scheme, the allocation of any amount of institutional costs to products is inherently arbitrary. For these reasons alone, the Commission cannot adopt UPS's regression-based approach. Additional defects, specific to UPS's regression-based approach are discussed below.

First, UPS regression-based approach attempts to link Competitive product volume and the Postal Service's institutional costs. However, its proposal is premised on the flawed assumption that there is a relationship between Competitive product volume and the Postal Service's institutional costs. Below, Figure VIII-5 illustrates changes in Competitive product volume compared to changes in the Postal Service's institutional costs since FY 2012.

²⁷³ See Sections VIII.A.3., VIII.B.3., VIII.C.3., *supra*. As stated above, 39 U.S.C. § 3622(b)(9) does not apply or require any regulatory action with respect to the Competitive product ratemaking system, and UPS's preferred interpretation would conflict with the Commission's express authority to eliminate the appropriate share under 39 U.S.C. § 3633(b). Additionally, UPS's regression-based approach does not account for the Postal Service's market power, the size of the overall parcel delivery market, or any other "prevailing competitive conditions in the market, and the degree to which any costs are uniquely or disproportionately associated with any competitive products." 39 U.S.C. § 3633(b).

²⁷⁴ UPS states that after costs are allocated to Competitive products and Market Dominant products based on its regression analysis, the remaining institutional cost would be allocated between Competitive products and Market Dominant products. UPS Comments at 62. Although UPS does not specify how this allocation should happen, UPS repeats that *all* institutional costs should be allocated between Competitive products and Market Dominant products. *Id.*

Figure VIII-5
Competitive Product Volume and Postal Service Institutional Cost,
FY 2012–FY 2021



Source: FY 2012 ACD; FY 2013 ACD; Library Reference PRC-LR-ACR2014/1; Library Reference PRC-LR-ACR2015/1; Library Reference PRC-LR-ACR2016/1; Library Reference PRC-LR-ACR2017-1; Library Reference PRC-LR-ACR2018-1; Library Reference USPS-FY19-1; Library Reference PRC-LR-ACR2020-1; Library Reference PRC-LR-ACR2021-1.

Figure VIII-5 illustrates the absence of correlation between rising Competitive product volumes and fluctuations in the Postal Service's institutional costs.²⁷⁵ Institutional costs have no discernable relationship to the provision of individual products or groups of products, so the regression methodology that UPS constructs is intended to link two values that are unrelated.

Second, the dependent variable in UPS's regression is *not* institutional costs, rather it is non-volume-variable costs. However, the Commission notes that these two types of costs are not synonymous because non-volume-variable costs include costs

²⁷⁵ See ASL Reply Comments at 24; Postal Service Reply Comments at 72-73; Pitney Bowes Reply Comments at 14-15.

that the Commission has already determined to have a causal relationship with Competitive products (*i.e.*, product-specific fixed and group-specific fixed costs). Therefore, setting aside the technical issues with UPS's regression-based approach, the choice of dependent variable effectively ensures that some correlation with Competitive products will be found because a portion of the costs that UPS's regression-based approach identifies are already attributed to Competitive products.

Third, the Commission finds that UPS's model relies on questionable data that are detrimental to the validity of its results. In particular, the Commission finds that the data series UPS constructs to represent non-volume-variable costs is problematic. UPS constructs four non-volume-variable cost series representing four categories of costs: delivery; clerks; transportation; and all other costs. Each series covers 8 years and is based on calculated values derived through the manipulation of the Postal Service's accrued costs. More specifically, UPS computes monthly workload-weighted volume figures by multiplying monthly volumes by FY 2021 annual unit costs. Commenters note, and the Commission agrees, that the development of monthly volume-variable costs by multiplying monthly volumes by annual unit costs was previously rejected by the Commission in Docket No. RM2020-9.²⁷⁶ As the Commission explained, such an approach fails to capture monthly differences in costs. See Order No. 6048 at 15.

Fourth, the Commission finds that UPS's model produces illogical results. For example, Dr. Bradley's analysis indicates that the variabilities implied by UPS's formulation fail to reflect reality. Bradley Report at 11. Using UPS's specifications, Dr. Bradley directly estimates accrued cost variability equations. *Id.* From there, he calculates the variabilities implied by the coefficients and compares them with

²⁷⁶ ASL Reply Comments at 24. As part of Docket No. RM2020-9, UPS proposed a similar methodology where it calculates monthly volume-variable costs for four aggregated cost categories (clerks, delivery, transportation, and other) by multiplying monthly volumes and annual unit costs. Order No. 6048 at 14. The only difference here is that UPS's proposal uses the same methodology to estimate monthly non-volume-variable costs. See UPS Comments at 57-63.

established variabilities. *Id.* He finds, and the Commission concurs, that the resulting variabilities for clerks and purchased transportation are unreasonably low when compared to the Commission's established variabilities. *Id.* The Commission finds that Dr. Bradley appropriately treats UPS's regressions as time series variability equations and agrees with his assessment that the variabilities implied by UPS's regressions "display a very unusual pattern and are at odds with operational experience." *Id.* Moreover, the Commission concurs with Dr. Bradley's conclusion that the "extreme variabilities call into question the accuracy and reliability of the UPS specification." *Id.* at 12.

Fifth, the Commission finds that the proposal is outside the scope of this proceeding. Instead of using the elements detailed in 39 U.S.C. § 3633(b) to determine the appropriate share that Competitive products should contribute to the Postal Service's institutional costs, UPS's regression-based approach appears to be an alternative to the Commission's cost attribution methodology. Several commenters also note that UPS's regression-based approach is an attempt to revisit the state of current cost attribution.²⁷⁷ With both Docket Nos. RM2016-2 and RM2020-9, UPS sought to attribute differing amounts of institutional costs to Competitive products.

Sixth, setting aside the flaws described above, the Commission acknowledges ASL's point that the results of UPS's regression-based approach would have a similar resulting appropriate share as the Commission's dynamic formula-based approach. See ASL Reply Comments at 26. For FY 2021, the Commission's dynamic formula-based approach would have required a minimum Competitive product contribution of

²⁷⁷ See Postal Service Reply Comments at 70 ("UPS mistakenly views the entire appropriate share review process, rather than as a pricing exercise for the purpose of determining appropriate shares of institutional costs, as merely an opportunity for a do-over of the costing function."); ASL Reply Comments at 23-24 (describing UPS's regression-based approach as a "warmed-over version" of UPS's proposals from Docket Nos. RM2016-2 and RM2020-9, which attempted to shift costs from the Postal Service's institutional costs to Competitive products' attributable costs and was rejected by the Commission).

\$3.1 billion,²⁷⁸ and UPS's regression-based approach would have required a minimum Competitive product contribution of \$3.8 billion (see UPS Comments at 62). Furthermore, as ASL notes, in FY 2021, Competitive products' institutional cost contribution "significantly exceeds" both of those values. See ASL Reply Comments at 26.

E. Elimination of the Appropriate Share

1. Introduction

In response to Order No. 3624, in which the Commission initiated the second periodic review and first requested feedback on the appropriate share requirement of 39 U.S.C. § 3633(a)(3), several commenters recommended that the Commission eliminate the appropriate share.²⁷⁹ These commenters generally maintain that the Postal Service does not have an unfair competitive advantage, and many assert that the Postal Service is operating at a competitive disadvantage. See Order No. 4402 at 89-90. Other commenters, such as UPS, opposed the elimination of the appropriate share requirement, asserting, among other things, that the appropriate share was necessary to ensure that the Postal Service competes on a level playing field.²⁸⁰

In Order No. 4402, the Commission found that the competitive market had and continued to develop and change, with the Postal Service gaining market power, market

²⁷⁸ Commission staff calculated 9.1 percent (the appropriate share for FY 2021 (Docket No. ACR2021, Library Reference PRC-LR-ACR2021-10, March 29, 2022, Excel file "PRC-LR-ACR2021-10.xlsx," tab "Appropriate Share Calculation," cell E15)) of \$33.6 billion (the institutional costs for FY 2021 (Library Reference PRC-LR-ACR2021-1, Excel file "21 Summary_LR1.xlsx," tab "Total All Mail (App'x A)," cell D78)).

²⁷⁹ See, e.g., Comments of Amazon Fulfillment Services, Inc., January 23, 2017, at 1; Declaration of John C. Panzar for Amazon Fulfillment Services, Inc., January 23, 2017, at 2; Initial Comments of the United States Postal Service, January 23, 2017, at 1.

²⁸⁰ See, e.g., Reply Comments of United Parcel Service, Inc. on Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products, March 9, 2017, at 7.

share, and growth in the market as a whole. Order No. 4402 at 96. Specifically, the Commission stated that “[t]he competitive market remain[ed] in a state of flux, innovation, and growth, with more efficient vehicles, dynamic routing algorithms, and Sunday delivery becoming increasingly common, and alternative forms of delivery (e.g., drone delivery) being explored.” *Id.* at 98. Although the Commission stated that it would consider the elimination of the appropriate share in future reviews as one of the options set forth in the plain language of 39 U.S.C. § 3633(b), for the reasons noted above, the Commission found that retaining the appropriate share and modifying it to capture market changes on an annual basis was the “best approach.” *Id.* at 98-99.

Commenters reiterated their positions in response to Order Nos. 4402 and 4742.²⁸¹ However, in Order No. 4963, after consideration of all commenters’ positions, the Commission continued to find that its dynamic formula-based approach was the most appropriate approach at that time. Order No. 4963 at 31.

²⁸¹ See, e.g., Comments of the United States Postal Service in Response to Order No. 4402, April 16, 2018, at 5-8; Comments of the United States Postal Service in Response to Order No. 4742, September 12, 2018, at 2, 5-6; Comments of Amazon.com Services, Inc. on Order No. 4402, April 16, 2018, at 6-40; Comments of Amazon.com Services, Inc. on Order No. 4742, September 12, 2018, at 5-6; Comments of the Parcel Shippers Association, April 16, 2018, at 1-3; Comments of Pitney Bowes Inc., April 16, 2018, at 4-13, 16; Comments of Pitney Bowes Inc. on Order No. 4742, September 12, 2018, at 3-4.

In response to Order No. 6043 (which reissued the dynamic formula-based approach), ASL, Pitney Bowes, the Postal Service, Dr. Panzar, the Public Representative, and PSA et al., continue to recommend that the Commission eliminate the appropriate share requirement of 39 U.S.C. § 3633(a)(3), whereas UPS continues to oppose elimination.²⁸²

2. Comments

The Public Representative, Dr. Panzar, Pitney Bowes, the Postal Service, and PSA et al. state that the minimum contribution requirement is unnecessary to promote fair competition, prevent cross-subsidization, or encourage the Postal Service to maximize contribution from Competitive products.²⁸³ Furthermore, Pitney Bowes, ASL, and PSA et al. note that there are inherent risks of setting the price floor of 39 U.S.C. § 3633(a)(3) too high, such as artificial price increases and market distortions.²⁸⁴

With respect to the commenters' argument that the Postal Service's natural incentive to maximize its profits renders it unnecessary for the Commission to set a minimum contribution requirement for Competitive products, UPS counters that "[t]his argument is baseless." UPS Reply Comments at 4. UPS contends that the Commission cannot assume that the Postal Service's natural incentive to maximize its profits will lead to the Postal Service "set[ting] prices for competitive products that will recover the maximum amount of institutional costs possible." *Id.* at 6. According to UPS, the Postal Service's natural incentive to profit-maximize is insufficient to ensure (what UPS considers to be) "[a]ppropriate [c]overage [o]f [i]nstitutional [c]osts." *Id.* at 4;

²⁸² See, e.g., ASL Comments at 1, 23-27, 46; ASL Reply Comments at 1, 4; PSA et al. Comments at 1, 7; Postal Service Comments at 1, 7-11; Postal Service Reply Comments at 3-6; Pitney Bowes Comments at 6-10; Pitney Bowes Reply Comments at 1, 8; PR Comments at 7; Panzar Decl. at 6-11; UPS Reply Comments at 4-13.

²⁸³ PR Comments at 7; Bowes Comments at 5, 7-9; Postal Service Comments at 7, 9-10; PSA et al. Comments at 1; Panzar Decl. at 6-11.

²⁸⁴ Pitney Bowes Comments at 9-10; ASL Comments at 24, 27; PSA et al. Comments at 6-7.

see *id.* at 4-11. UPS repeats its position that the appropriate share is necessary to ensure a level playing field and prevent the Postal Service from engaging in “strategies that allow it to exploit its status as a government-sponsored monopolist” *Id.* at 13-16.

3. Commission Analysis

The Commission has considered the alternative of eliminating the appropriate share. First, the Commission acknowledges commenters’ concerns about setting the appropriate share too high. However, given that Competitive product contribution has consistently exceeded the formula-based appropriate share percentage, the Commission finds that its dynamic formula-based approach poses little to no risk of irrational price increases or market distortions.²⁸⁵ The commenters favoring elimination recognize this to be the case.²⁸⁶ Based on the historical changes in the appropriate share percentage, the Commission finds it unlikely that Competitive products would be restrained by the appropriate share unexpectedly. The Commission reviews the Postal Service’s finances each year during its annual compliance review process. The Commission will monitor the difference between the appropriate share produced by its dynamic formula-based approach and Competitive contribution. If the Postal Service’s pricing behavior changes or contribution to institutional costs begin to decline, the Commission retains the authority to revisit the appropriate share requirement at any time to reassess the relevant circumstances of 39 U.S.C. § 3633(b). See Order No.

²⁸⁵ See Order No. 6043 at 93. The Commission has previously explained that Competitive product contribution to institutional costs has always exceeded the amount required under the appropriate share, often by a significant margin. See *id.*; FY 2021 ACD at 94-100; FY 2020 ACD at 91-95; FY 2019 ACD at 86-89; FY 2018 ACD at 112-17; Order No. 4402 at 52-53.

²⁸⁶ PR Comments at 7; Pitney Bowes Comments at 5, 7-9, 9-10; Postal Service Comments at 7, 9-10; ASL Comments at 24, 27; PSA et al. Comments at 1, 6-7; Panzar Decl. at 6-11.

6043 at 94-95. Thus, the Commission would be able to reevaluate the appropriateness of its dynamic formula-based approach before any harm could occur.

Second, despite UPS's suggestion otherwise, the appropriate share provision does not direct the Commission to ensure that the Postal Service maximizes its profits. The PAEA granted the Postal Service pricing flexibility over its Competitive products, subject to minimal regulatory oversight by the Commission (as compared to Market Dominant products, which are subject to a price cap and constraints on the relationships between certain rates).²⁸⁷ Although the Commission chooses to retain the appropriate share, its intention in doing so (consistent with the PAEA) is to strike a balance between preventing unfair competition in the market for competitive postal services while at the same time not unduly restraining competitive conduct in the market by the Postal Service. Because the PAEA permits the Postal Service to retain earnings from Competitive products, the Postal Service is incentivized to maximize contribution from Competitive products. Order No. 6043 at 60; Section IV.B.2., *supra*.

Third, the Commission acknowledges that it indeed has the express authority to eliminate the appropriate share requirement of 39 U.S.C. § 3633(a)(3), if the Commission determines that the relevant circumstances, including the prevailing competitive conditions in the market, warrant doing so. Order No. 6043 at 59-60. Thus, unlike the prohibitions against subsidization appearing in 39 U.S.C. § 3633(a)(1) and (a)(2), the appropriate share requirement is not necessarily a permanent component of Competitive product regulation. *Id.* at 60. Having said that, the Commission continues to find that the market conditions underlying the original 5.5 percent appropriate share have changed, and that the Commission's dynamic formula-based approach will better capture the statutory criteria of 39 U.S.C. § 3633(b) than making other modifications to, eliminating, or maintaining the 5.5 percent appropriate share would. Although the

²⁸⁷ See 39 U.S.C. §§ 3622(d)-(e), 3626. See also Order No. 6043 at 43; Section IV.B.2., *supra*.

Commission does not find that elimination of the appropriate share is the most appropriate course of action at this juncture considering current market conditions, the Commission will consider it in future reviews as one of the options expressly authorized by 39 U.S.C. § 3633(b). At this juncture, the Commission's determination to retain the appropriate share serves as a margin of safety against any possibility of the Postal Service having an unfair competitive advantage. *Id.* at 95.

IX. REGULATORY FLEXIBILITY ACT ANALYSIS

The Regulatory Flexibility Act requires Federal agencies, in promulgating rules, to consider the impact of those rules on small entities. See 5 U.S.C. §§ 601, *et seq.* If the proposed or final rules will not, if promulgated, have a significant economic impact on a substantial number of small entities, the head of the agency may certify that the initial and final regulatory flexibility analysis requirements of 5 U.S.C. §§ 603 and 604 do not apply. See 5 U.S.C. § 605(b). In the context of this rulemaking, the Commission's primary responsibility is in the regulatory oversight of the United States Postal Service. The rule that is the subject of this rulemaking has a regulatory impact on the Postal Service, but it does not impose any regulatory obligation upon any other entity. Based on these findings, the Chairman of the Commission certifies that the rule that is the subject of this rulemaking will not have a significant economic impact on a substantial number of small entities. Therefore, pursuant to 5 U.S.C. § 605(b), this rulemaking is exempt from the initial and final regulatory flexibility analysis requirements of 5 U.S.C. §§ 603 and 604.

X. ORDERING PARAGRAPHS

It is ordered:

1. Part 3035 of title 39, Code of Federal Regulations, is amended as set forth below the signature of this Order effective 30 days after the date of publication of the final rule in the *Federal Register*.
2. The Secretary shall arrange for publication of the final rule and general statement as to the basis and purpose of the final rule in the *Federal Register*.
3. The Motion of the United States Postal Service for Leave to File Reply Comments Regarding Order No. 6269, filed September 30, 2022, is granted.

By the Commission.

Erica A. Barker
Secretary

List of Subjects for 39 CFR Part 3035

Administrative practice and procedure.

For the reasons stated in the preamble, the Commission amends chapter III of title 39 of the Code of Federal Regulations as follows:

PART 3035—REGULATION OF RATES FOR COMPETITIVE PRODUCTS

1. The authority citation for part 3035 continues to read as follows:

Authority: 39 U.S.C. 503; 3633.

2. Amend § 3035.107 by revising paragraph (c) to read as follows:

§ 3035.107 Standards for compliance.

* * * * *

(c)(1) Annually, on a fiscal year basis, the appropriate share of institutional costs to be recovered from competitive products collectively, at a minimum, will be calculated using the following formula:

$$AS_{t+1} = AS_t * (1 + \% \Delta CCM_{t-1} + CGD_{t-1})$$

Where,

AS = Appropriate Share, expressed as a percentage and rounded to one decimal place

CCM = Competitive Contribution Margin

CGD = Competitive Growth Differential

t = Fiscal Year

If $t = 0$ = FY 2007, AS = 5.5 percent

(2) The Commission shall, as part of each Annual Compliance Determination, calculate and report competitive products' appropriate share for the upcoming fiscal year using the formula set forth in paragraph (c)(1) of this section.

APPENDIX A
INITIAL, REPLY, AND SECTION 703 COMMENTS AND RELATED FILINGS

Commenter(s)	Citation	Citation Short Form
American Consumer Institute (ACI)	Comments of American Consumer Institute Center for Citizen Research Regarding Docket No. RM2022-2, Submitted to the United States Postal Regulatory Commission, March 25, 2022.	ACI Reply Comments
Amazon.com Services LLC (ASL)	Comments of Amazon.com Services LLC, February 25, 2022.	ASL Comments
	Declaration of John C. Panzar for Amazon.com Services LLC, February 25, 2022.	Panzar Decl.
	Declaration of John W. Mayo, February 25, 2022.	Mayo Decl.
	Library Reference ASL-LR-RM2022-2/1, February 25, 2022. ¹	Library Reference ASL-LR-RM2022-2/1
	Library Reference ASL-LR-RM2022-2/2, February 25, 2022. ²	Library Reference ASL-LR-RM2022-2/2
	Reply Comments of Amazon.com Services LLC, March 25, 2022.	ASL Reply Comments
	Reply Declaration of John C. Panzar for Amazon.com Services LLC, March 25, 2022.	Panzar Reply Decl.
	Library Reference ASL-LR-RM2022-2/3, March 25, 2022. ³	Library Reference ASL-LR-RM2022-2/3
	Comments of Amazon.com Services LLC, September 21, 2022.	ASL 703(d) Comments
Lexington Institute (LI)	Comments of the Lexington Institute, February 25, 2022.	LI Comments

¹ This public library reference was accompanied by a notice of filing and consists of two files: PDF file "ASL-LR-RM2022-2-1.pdf" and Excel file "ASL-LR-RM2022-2-1.xlsx." Notice of Amazon.com Services LLC of Filing of Library Reference ASL-LR-RM2022-2/1, February 25, 2022.

² This public library reference was accompanied by a notice of filing and consists of an Excel file "ASL-LR-RM2022-2-2.xlsx." Notice of Amazon.com Services LLC of Filing of Library Reference ASL-LR-RM2022-2/2, February 25, 2022.

³ This public library reference was accompanied by a notice of filing and consists of an Excel file "ASL-LR-RM2022-2-3.xlsx." Notice of Amazon.com Services LLC of Filing of Library Reference ASL-LR-RM2022-2/3, March 25, 2022.

Commenter(s)	Citation	Citation Short Form
Package Shippers Association, American Catalog Mailers Association, Association for Mail Electronic Enhancement, ANA—Association of National Advertisers, Continuity Shippers Association, Envelope Manufacturers Association, International Mailers Advisory Group, Mailers Hub, Major Mailers Association, National Association of Presort Mailers, and Printing United Alliance (PSA et al.)	Comments of Package Shippers Association, American Catalog Mailers Association, Association for Mail Electronic Enhancement (AMEE), ANA—Association of National Advertisers, Continuity Shippers Association, Envelope Manufacturers Association, International Mailers Advisory Group, Mailers Hub, Major Mailers Association, National Association of Presort Mailers, and Printing United Alliance ("PSA, et al."), February 25, 2022.	PSA et al. Comments
	Library Reference PSA et al-LR-RM2022-2/1, February 25, 2022. ⁴	Library Reference PSA et al-LR-RM2022-2/1
	Comments of the Package Shippers Association, September 21, 2022.	PSA 703(d) Comments
Pitney Bowes Inc. (Pitney Bowes)	Comments of Pitney Bowes Inc., February 25, 2022.	Pitney Bowes Comments
	Reply Comments of Pitney Bowes Inc., March 25, 2022.	Pitney Bowes Reply Comments
	Comments of Pitney Bowes Inc., September 21, 2022.	Pitney Bowes 703(d) Comments
Public Representative (PR)	Public Representative Comments, February 25, 2022.	PR Comments
	Public Representative Reply Comments, March 25, 2022.	PR Reply Comments
	Public Representative Comments, September 21, 2022.	PR 703(d) Comments

⁴ This public library reference was accompanied by a notice of filing and consists of an Excel file, "PSA et al-LR-RM2022-2_1.xlsx." Notice of Package Shippers Association, American Catalog Mailers Association, Association for Mail Electronic Enhancement (AMEE), ANA—Association of National Advertisers, Continuity Shippers Association, Envelope Manufacturers Association, International Mailers Advisory Group, Mailers Hub, Major Mailers Association, National Association of Presort Mailers, and Printing United Alliance ("PSA, et al.") of Filing of Library Reference PSA et al-LR-RM2022-2/1, February 25, 2022.

Commenter(s)	Citation	Citation Short Form
United Parcel Service, Inc. (UPS)	Initial Comments of United Parcel Service, Inc. on Supplemental Notice of Proposed Rulemaking and Order Initiating the Third Review of the Institutional Cost Contribution Requirement for Competitive Products, February 25, 2022.	UPS Comments
	Library Reference UPS-LR-RM2022-2/NP1, February 25, 2022. ⁵	Library Reference UPS-LR-RM2022-2/NP1
	Reply Comments of United Parcel Service, Inc. on Supplemental Notice of Proposed Rulemaking and Order Initiating the Third Review of the Institutional Cost Contribution Requirement for Competitive Products, March 25, 2022.	UPS Reply Comments
	Library Reference UPS-LR-RM2022-2/NP2, March 25, 2022. ⁶	Library Reference UPS-LR-RM2022-2/NP2
	Comments of United Parcel Service, Inc. in Response to Notice and Order Providing an Opportunity to Comment on the Commission's Section 703(d) Analysis, September 21, 2022.	UPS 703(d) Comments
United States Postal Service (Postal Service)	Initial Comments of the United States Postal Service in Response to Order No. 6043, February 25, 2022.	Postal Service Comments
	Reply Comments of the United States Postal Service in Response to Order No. 6043, March 25, 2022.	Postal Service Reply Comments
	Professor Michael D. Bradley, Department of Economics, George Washington University, Analysis of UPS' Regression-Based Approach to Identify Costs Associated with Competitive Products, March 25, 2022. ⁷	Bradley Report
	Comments of the United States Postal Service in Response to Order No. 6269, September 21, 2022.	Postal Service 703(d) Comments
	Reply Comments of the United States Postal Service Regarding Order No. 6269, September 30, 2022.	Postal Service 703(d) Reply Comments
Taxpayers Protection Alliance (TPA)	Comments of the Taxpayers Protection Alliance, March 25, 2022.	TPA Reply Comments

Note: Declarations, library references, and reports are organized above by the sponsoring participant.

⁵ UPS filed this material under seal and sought non-public treatment. Notice of Filing of Library Reference UPS-LR-RM2022-2/NP1 and Application for Nonpublic Treatment, February 25, 2022.

⁶ UPS filed this material under seal and sought non-public treatment. Notice of Filing of Library Reference UPS-LR-RM2022-2/NP2 and Application for Nonpublic Treatment, March 25, 2022.

⁷ This public material consists of two files: PDF file "Bradly.Report.UPS.NVVC.Regressions.pdf" and ZIP file "USPS_Bradley.Reply.Programs and Data.zip."

APPENDIX B
MOTIONS PRACTICE AND RELATED FILINGS

Filings Related to Access to Non-Public Library Reference UPS-LR-RM2022-2/NP1:

Motion of the United States Postal Service for Access to UPS-LR-RM2022-2/NP1, February 28, 2022.

Amazon.com Services LLC's Motion Requesting Access to Non-Public Materials Under Protective Conditions, February 28, 2022.

Order Granting Motions for Access, March 1, 2022 (Order No. 6112) (granting the Postal Service's and ASL's uncontested motions granting access to non-public Library Reference UPS-LR-RM2022-2/NP1).

Filings Related to Access to Non-Public Library Reference UPS-LR-RM2022-2/NP2:

Motion of the United States Postal Service for Access to UPS-LR-RM2022-2/NP2, March 28, 2022.

Amazon.com Services LLC's Motion Requesting Access to Non-Public Materials Under Protective Conditions, March 28, 2022.

Order Granting Motions for Access, March 29, 2022 (Order No. 6126) (granting the Postal Service's and ASL's uncontested motions granting access to non-public Library Reference UPS-LR-RM2022-2/NP2).

Filings Related to Information Requests:

Motion of the United States Postal Service for Issuance of an Information Request to United Parcel Service, Inc., March 2, 2022.

Chairman's Information Request No. 1, March 3, 2022.

Responses of United Parcel Service, Inc. to Chairman's Information Request No. 1, March 10, 2022.

Other Motions:

Motion of the United States Postal Service for Leave to File Reply Comments Regarding Order No. 6269, September 30, 2022 (Postal Service Motion for Leave).